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Supreme Court, U.S.
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No. 92-

IN THE

Supreme Court of the United States

OCTOBER TERM, 1992

NATIONWIDE CORPORATION and
NATIONWIDE MUTUAL INSURANCE COMPANY,
Petitioners,

v.

HOWING COMPANY and
DOUGLAS MCLELLAN,
Respondents.

Petition for a Writ of Certiorari to the United States Court of Appeals for the Sixth Circuit

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PETITION FOR A WRIT OF CERTIORARI

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QUESTIONS PRESENTED

This petition presents three important questions involving (1) *implied private damages actions* and standards of (2) *materiality* and (3) *causation* in the context of a proxy statement issued under the federal securities laws. This Court has previously determined that the first two questions warrant certiorari in this case. *See Nationwide Corp. v. Howing Co.*, 112 S. Ct. 39 (1991) (Order granting certiorari, vacating and remanding for further consideration the Sixth Circuit's decisions on the implied damages action and materiality questions in light of *Virginia Bankshares, Inc. v. Sandberg*, 111 S. Ct. 2749 (1991)). But on remand, the Sixth Circuit refused to re-examine these questions and summarily reaffirmed its prior decisions. The third question involves the lost state remedies causation issue that this Court expressly left open in *Virginia Bankshares* and the Sixth Circuit resolved on remand. Like *Virginia Bankshares*, all three questions involve a consideration of state law issues, particularly to the extent that the Sixth Circuit has intertwined federal securities law issues with state law.

1. Can the Sixth Circuit enlarge the contemporary legal context test of *Cannon v. University of Chicago* to presume an implied damages action for every statute enacted between 1916 and 1975, including Section 13(e)(1) of the Securities Exchange Act of 1934, where that decision:

> (a) is contrary to this Court's decisions in *Transamerica Mortgage Advisors, Inc. v. Lewis*, *Touche Ross & Co. v. Redington* and *Virginia Bankshares* that federal courts should not imply private damages actions where, as here, the legislative history is silent;
>
> (b) conflicts with Second and Third Circuit authority that, notwithstanding *Cannon*, the courts must apply the current test for implying damages actions rather than the one in vogue when the statute was passed; and

(c) conflicts with other, better-reasoned federal court decisions relying on *Transamerica* and *Touche Ross* to reject private damages actions under Section 13 (e)(1)?

2. Can the Sixth Circuit create a *presumption* that omission of any information required by SEC regulation or from a proxy statement in a going-private merger must be deemed *material* where that decision:

(a) is contrary to this Court's decisions in *TSC Indus., Inc. v. Northway, Inc.*, *Basic Inc. v. Levinson* and *Virginia Bankshares* that information is material only if a reasonable shareholder would have placed actual significance on the omitted information, even in cases involving going-private mergers; and

(b) conflicts with other, better-reasoned federal appellate decisions in the D.C., First, Second and Seventh Circuits applying the *TSC* materiality standard even in cases involving omissions of information required by SEC regulation or going-private mergers?

3. Can the Sixth Circuit resolve the *causation* question expressly left open in *Virginia Bankshares* to permit recovery in federal court for lost state remedies where that decision:

(a) is contrary to the analysis mandated in *Virginia Bankshares* that causation cannot be established on a lost state remedies theory where, as here, there is no indication in the facts or law that the proxy solicitation resulted in any such loss; and

(b) is inconsistent with this Court's precedents denying federal securities law claims based on hazy, speculative proof and unnecessary to the fulfillment of federal policy?

PARTIES TO THE PROCEEDINGS

Petitioners Nationwide Corporation and Nationwide Mutual Insurance Company were the appellees in the Court of Appeals. Respondents Howing Company and Douglas McLellan were the appellants below.

Pursuant to Supreme Court Rule 29.1, petitioners make the following disclosure: Nationwide Corporation is owned by Nationwide Mutual Insurance Company and Nationwide Mutual Fire Insurance Company, both of which are mutual insurance companies owned by their respective policyholders. At the present time, the subsidiaries (except wholly-owned subsidiaries) and affiliates of Nationwide Corporation, Nationwide Mutual Insurance Company or Nationwide Mutual Fire Insurance Company are: Employers Insurance of Wausau A Mutual Company, Wausau County Mutual Insurance Company, Greater La Crosse Health Plans, Inc., Wausau Lloyds, Allnations, Inc., Farmland Mutual Insurance Company, Nationwide Agribusiness Insurance Co., NGC County Mutual Insurance Company, Nationwide Investing Foundation, Nationwide Investing Foundation II, Nationwide Separate Account Trust, Financial Horizons Investment Trust and Financial Horizons Distributors Agency of Ohio, Inc.

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PETITION FOR A WRIT OF CERTIORARI

Petitioners, Nationwide Corporation and Nationwide Mutual Insurance Company, respectfully request that a writ of certiorari issue to review the judgments and decisions of the U.S. Court of Appeals for the Sixth Circuit entered August 17, 1992, March 6, 1991 and August 7, 1987.

OPINIONS BELOW

The most recent opinion of the panel below and Judge Guy's dissent are published at *Howing Co. v. Nationwide Corp.*, 972 F.2d 700 (6th Cir. 1992) (*"Howing III"*) and appear in the appendix at pp. 1a-25a, *infra*. Those opinions were in response to this Court's Order granting certiorari, vacating the Sixth Circuit's prior two opinions and remanding for reconsideration in light of *Virginia Bankshares, Inc. v. Sandberg*, 111 S. Ct. 2749 (1991). *See* 112 S. Ct. 39 (1991). The majority opinion focuses on the issue of whether a lost state remedies theory can be used to establish causation under the federal securities laws.

The previous opinion of the panel majority and Judge Guy's dissent are published at *Howing Co. v. Nationwide Corp.*, 927 F.2d 263 (6th Cir. 1991) (*"Howing II"*) and appear in the appendix at pp. 29a-41a, *infra*. Those opinions involve whether the materiality of an alleged nondisclosure can be presumed under the securities laws. The District Court opinion on that issue is published at *Howing Co. v. Nationwide Corp.*, 1989-90 Fed. Sec. L. Rep. (CCH) ¶ 94,858 (S.D. Ohio 1989), and appears in the appendix at pp. 43a-61a, *infra*.

The first opinion of the Sixth Circuit and Judge Guy's opinion dissenting in part are published at *Howing Co. v. Nationwide Corp.*, 826 F.2d 1470 (6th Cir. 1987) (*"Howing I"*), and appear in the appendix at pp. 62a-95a, *infra*. Those opinions involve whether a private damages action can be implied under Section 13(e)(1) of the Securities Exchange Act. The District Court opinion on that issue is published at *Howing Co. v. Nationwide*

Corp., 625 F. Supp. 146 (S.D. Ohio 1985), and appears in the appendix at pp. 96a-117a, *infra*.

JURISDICTION

The most recent decision of the Sixth Circuit was entered on August 17, 1992. On November 4, 1992, the Sixth Circuit denied petitioners' timely filed motion for rehearing with suggestion for rehearing *en banc*. The Sixth Circuit's initial decision was entered on August 7, 1987, and its second decision on March 6, 1991. Petitioners invoke the jurisdiction of this Court to review all three decisions under 28 U.S.C. § 1254(1) (1988). *See Mercer v. Theriot*, 377 U.S. 152 (1964) (Court can consider questions decided in earlier court of appeals' opinion). The District Court's jurisdiction was invoked under 15 U.S.C. § 78aa and 28 U.S.C. §§ 1331, 1332 (1988), as well as principles of pendent jurisdiction.

STATUTORY AND REGULATORY PROVISIONS INVOLVED

This case involves the following statutory and regulatory provisions which are set out in the appendix at pp. 118a-120a, *infra*: Section 13(e)(1) of the Securities Exchange Act of 1934, 15 U.S.C. § 78m(e)(1) (1988); Section 18(a) of the Securities Exchange Act of 1934, 15 U.S.C. § 78r(a) (1988); and Rule 13e-3(b)(1), 17 C.F.R. § 240.13e-3(b)(1) (1990).

STATEMENT OF THE CASE

Factual History

As of 1982, Nationwide Mutual Insurance Co. and its affiliate Nationwide Mutual Fire Insurance Co. owned 85.6 percent of the Class A stock and 100 percent of the Class B stock of Nationwide Corp. (JA 296.)[1] In 1982, Nationwide Mutual approached Nationwide Corp. to propose a going-private merger whereby Nationwide Mu-

[1] References to "JA" are to the Sixth Circuit Joint Appendix filed by the parties on July 19, 1990. References to "SA" are to the Sixth Circuit Supplemental Appendix filed on January 21, 1992.

tual would acquire the remaining Class A stock from the public stockholders. (JA 297.) Nationwide Mutual and Nationwide Corp. took extraordinary steps to ensure the fairness of any merger to Nationwide Corp.'s public stockholders: (1) a leading investment banking firm (The First Boston Corporation) was hired to represent the public stockholders and given complete discretion to pick the price it deemed fair to those stockholders; (2) independent legal counsel was retained to represent the public stockholders; (3) an Evaluation Committee comprised of independent Nationwide Corp. directors was created to examine the fairness of the transaction to the public stockholders; and (4) a majority of the Nationwide Corp. directors voting on the transaction was disinterested. (JA 51-52, 250-60.)

After a month-long study, First Boston concluded that $42.50 per share—51.8 percent over the market price of the stock—was the fair price. (JA 239-45, 251-60.) The fairness of the price was next evaluated by the Evaluation Committee, which concluded that First Boston's investigation had been thorough and that its conclusions were sound. (JA 265-68, 272.) Accordingly, the Evaluation Committee voted unanimously to approve the merger. (JA 269, 392.) After considering reports from First Boston and the Evaluation Committee, the full Board voted unanimously in favor of the merger. (JA 241, 245, 298.)

Ultimately, the transaction was presented to the Nationwide Corp. stockholders for approval. Nationwide Mutual's ownership of more than a majority of the stock assured that the transaction would receive the approval required by state law and Nationwide Corp.'s articles of incorporation. (JA 122, 138); Ohio Rev. Code Ann. § 1701.78(F) (Anderson 1992). Nationwide Corp. issued a proxy statement fully informing the shareholders of their appraisal rights and told the shareholders precisely how to seek an appraisal in the event that they chose to do so. (*See* JA 97-98.) The shareholders were specifically told that, under this procedure, each of them was "en-

titled to a court determination of the fair cash value of such shares as a dissenting shareholder under Ohio law." (*Id.* at 97.)

The merger was approved overwhelmingly; over 94 percent of the publicly held shares that voted (and 75 percent of *all* the publicly held shares) favored the merger. (JA 61.) Plaintiffs did not vote (JA 246), and thereby preserved their appraisal rights. *See* Ohio Rev. Code Ann. § 1701.85. Plaintiff McLellan admitted he was "aware that under Ohio law with respect to the merger that [he] had appraisal rights as a stockholder of Nationwide Corporation" and that he "elected not to pursue those appraisal rights . . . even though [he] believed that the $42.50 merger price was inadequate." (SA 623.) Likewise, plaintiff Howing Company, through its managing partner, admitted that it did not "seek to exercise its appraisal rights" because "there was already a litigation started as a class action suit" and "there was no point in going after" appraisal rights. (SA 627-28, 630-31.) Plaintiffs' counsel also acknowledged that his clients had consciously elected not to pursue their appraisal rights based on litigation tactics. (SA 633-36.) Based on this record, the District Court found that plaintiffs "could have" pursued their appraisal rights but "have chosen" not to do so. (SA 641.)

Procedural History

Plaintiffs filed suit in 1983, raising a host of challenges to the merger under seven federal securities laws and regulations. In 1985, the District Court granted petitioners' first summary judgment motion. *See* 625 F. Supp. 146. On plaintiffs' first appeal, the Sixth Circuit affirmed the dismissal of all but one of plaintiffs' securities law claims. As to the remaining claim, the panel majority (with Judge Guy dissenting) ruled that plaintiffs did have an implied damages action under Section 13(e)(1). *See Howing I*, 826 F.2d at 1476. The divided panel further ruled that the proxy statement should have disclosed Nationwide Corp.'s assessment of book, liquidation and going concern value—three items mentioned in

Schedule 13E-3, Item 8(b) promulgated pursuant to SEC Rule 13e-3(b)(1)—and remanded the case to the District Court to "consider issues of materiality of the defendants' omission." 826 F.2d at 1481.

On remand, the District Court addressed the materiality issues, finding that since the omitted assessments "all resulted in amounts less than the cash out price of $42.50," the disclosure of such information "would not have significantly altered the 'total mix' of information available to the shareholders in deciding how to vote on the merger issue." *See* 1989-90 Fed. Sec. L. Rep. at 94,653 (citing *TSC Indus., Inc. v. Northway, Inc.*, 426 U.S. 438, 449 (1976)). Summary judgment was therefore entered in petitioners' favor. Plaintiffs appealed to the Sixth Circuit a second time. On March 6, 1991, a divided panel reversed the District Court's ruling that any omission was immaterial to plaintiffs' Section 13(e)(1) claim. *See Howing II*, 927 F.2d 263. Judge Guy again dissented. *Id.* at 270. The panel majority concluded that because disclosure of the three valuation items was required by Item 8 of the Schedule 13E-3, the information was "presumptively" material, thus precluding summary judgment. *Id.* at 266-67.

On June 4, 1991, Nationwide petitioned this Court for a writ of certiorari on the materiality and private right of action issues. After the filing of the petition, the Court issued its opinion in *Virginia Bankshares v. Sandberg*, 111 S. Ct. 2749 (1991). On October 7, 1991, this Court granted certiorari on the two questions presented, vacated the Sixth Circuit's judgment and remanded for consideration in light of *Virginia Bankshares*. *See* 112 S. Ct. 39. On remand, the Sixth Circuit summarily reaffirmed the private right of action and materiality decisions of *Howing I* and *II* without any indication of how those determinations could be reconciled with *Virginia Bankshares*. *See Howing III*, 972 F.2d 700. The panel majority focused its opinion on the lost state remedies causation issue left open in *Virginia Bankshares*. Judge Guy again dissented. *Id.* at 710-12.

REASONS FOR GRANTING THE WRIT

As this Court's October 7, 1991 Order granting certiorari on the implied private damages action and materiality issues indicates, these two questions meet the traditional standards set forth in Supreme Court Rule 10.1(a) and (c) for exercise of this Court's jurisdiction. The third question presented by this petition—the challenge to the Sixth Circuit's creation of a new theory of causation—likewise meets those standards. All three questions involve the decision of a federal question in conflict with decisions of this Court and with other federal courts of appeals. The issues also have great significance for the administration of the federal securities laws, for the regulation of going-private mergers and to the public at large. Finally, the causation issue was explicitly left open in *Virginia Bankshares*, presenting an important question of federal law which has not been, but should be, settled by this Court.

I. The Sixth Circuit's recognition of a private right of action under Section 13(e)(1) satisfies the standards for certiorari since it is inconsistent with the decisions of this Court and conflicts with better-reasoned decisions from lower federal courts. *First*, the Sixth Circuit's conclusion that Congressional silence supports the implication of a private right of action is contrary to this Court's directives, first announced in *Touche Ross & Co. v. Redington*, 442 U.S. 560 (1979), and *Transamerica Mortgage Advisors, Inc. v. Lewis*, 444 U.S. 11 (1979), and recently reaffirmed in *Virginia Bankshares, Inc. v. Sandberg*, 111 S. Ct. 2749 (1991), which require affirmative evidence of Congressional intent to establish implied damages actions. *Second*, the Sixth Circuit dramatically expanded the "contemporary legal context" doctrine announced in *Cannon v. University of Chicago*, 441 U.S. 677 (1979), in a manner inconsistent with the decisions of this Court in *Transamerica*, *Touche Ross* and *Virginia Bankshares* by presuming that virtually all statutes enacted prior to 1975 have an implied cause of action. The Sixth Circuit's recognition of an implied cause of action also establishes

a conflict with other courts of appeals which have held that, notwithstanding *Cannon*, courts must apply the Supreme Court's current test for implying damages actions rather than the one in place when the statute was passed. *See Siebert v. Conservative Party*, 724 F.2d 334, 337 (2d Cir. 1983), *cert. denied*, 466 U.S. 980 (1984); *American Tel. & Tel. Co. v. M/V Cape Fear*, 976 F.2d 864, 871-72 (3d Cir. 1992). *Finally*, this Court's guidance is needed to resolve the conflict in the lower courts regarding whether Section 13(e)(1) contains an implied damages action. *See Kalmanovitz v. G. Heileman Brewing Co.*, 595 F. Supp. 1385, 1395 (D. Del. 1984) (no private right of action under Section 13(e)), *aff'd*, 769 F.2d 152 (3d Cir. 1985); *Berg v. First American Bankshares, Inc.*, 1984-85 Fed. Sec. L. Rep. (CCH) ¶ 92,011 at 91,013 (D.D.C. 1985) (same), *aff'd*, 796 F.2d 489 (D.C. Cir. 1986).

The numerous decisions of this Court granting certiorari to review opinions implying private causes of action in federal statutes demonstrate the critical importance of such questions.[2] Because the Sixth Circuit's extension of *Cannon* will have far-reaching legal implications not just in the Section 13(e)(1) context, but for other statutes as well, this Court should grant the petition for a writ of ceriorari as to this issue.

II. The Sixth Circuit's presumption of materiality is contrary to decisions of this Court and the federal courts of appeals. In *TSC Indus., Inc. v. Northway, Inc.*, 426 U.S. 438 (1976), and *Basic Inc. v. Levinson*, 485 U.S. 224 (1988), the Court announced a uniform standard for judging materiality under the securities laws. Information that is of "dubious significance" in that it does not alter the " 'total mix' of information made available" is immaterial and does not give rise to liability. *TSC*, 426

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[2] *See, e.g., Transamerica*, 444 U.S. at 14 (existence of implied cause of action is an "important federal question"); *Touche Ross*, 442 U.S. at 562 & n.1 (certiorari granted in five cases raising issue of implied causes of action in one term alone).

U.S. at 448, 449. Under *TSC*, that determination is made by scrutinizing the information in the fact-specific context of "all the circumstances" of the pending transaction. *Id.* at 449. In *Basic*, this Court reaffirmed the *TSC* standard and rejected adoption of a different standard for cases such as going-private mergers in which insiders are alleged to have greater access to information. 485 U.S. at 240 n.18. That holding was reaffirmed in *Virginia Bankshares*, which applied the *TSC* standard to a proxy statement in connection with a going-private merger. In contrast, the Sixth Circuit relied on its view of going-private mergers as "coercive securities transactions" to conclude that *TSC* was not controlling and that information must be *presumed* to be material regardless of the specific circumstances of the pending transaction if it is the subject of an SEC regulation.

Other courts of appeals have consistently applied the *TSC* standard to judge materiality under *all* provisions of the federal securities laws. The Sixth Circuit's decision that a different standard applies to Section 13(e)(1) creates a direct conflict with the D.C. Circuit. *See Berg v. First American Bankshares, Inc.*, 796 F.2d 489, 495, 502 (D.C. Cir. 1986). The Sixth Circuit's conclusion that a different materiality standard applies in cases involving information contemplated by an SEC rule or a going-private merger also creates a conflict with leading appellate decisions refusing to depart from the *TSC* standard in those settings, including *United States v. Bilzerian*, 926 F.2d 1285, 1298-99 (2d Cir.), *cert. denied*, 112 S. Ct. 63 (1991).

This case has exceptional importance. During the last three years for which statistics are available, 7481 securities actions were filed in the federal district courts.[3] Materiality is frequently an issue in such cases, as evidenced by the fact that 185 of the cases reported during

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[3] *Reports of the Proceedings of the Judicial Conference of the United States: Annual Report of the Director of the Administrative Office of the United States Courts*, at 193 (1991).

that time included a discussion of that issue.[4] Year after year, there are a large number of proxy statements that can become subject to attack under the Sixth Circuit's reasoning. During the last three years alone, 597 proxy statements were filed with the SEC describing going-private mergers.[5] Such transactions involve a substantial volume of commerce: over $22.4 billion during the last three years, constituting 16.5% of all public takeovers.[6] In addition, there are approximately 179 forms and schedules promulgated by the SEC just under the 1933 and 1934 Acts that would be subject to the Sixth Circuit's presumption of materiality. The Sixth Circuit's decision thus creates enormous uncertainty for innumerable securities cases and transactions by holding that the *TSC* standard no longer is controlling where going-private transactions or SEC schedules are involved.

III. The Sixth Circuit's adoption of a novel lost state remedies theory of causation conflicts with decisions of this Court and other courts of appeals. *First*, the Sixth Circuit's decision is contrary to the analysis mandated in *Virginia Bankshares* that causation cannot be established where, as here, there "is no indication in the law or facts" that a "proxy solicitation resulted in any such loss." 111 S. Ct. at 2766. The Sixth Circuit never challenged or set aside the District Court's finding, based on the admissions of plaintiffs and their counsel, that there was no loss of appraisal rights or other state remedy. This case is thus indistinguishable from *Virginia Bankshares*. The Sixth Circuit's interpretation of *Virginia*

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[4] 1989, 1990, 1991 LEXIS Genfed library, Courts file.

[5] *SEC Budget Estimate for Fiscal Year 1991: Hearings Before a Subcomm. of the Comm. on Appropriations*, 101st Cong., 2d Sess. 1299, 1327 (1990) (detailing actual filings in 1989); *SEC Budget Estimate for Fiscal Year 1992: Hearings before a Subcomm. of the Comm. on Appropriations*, 102d Cong., 1st Sess. 501, 527 (1991) (same for 1990); *SEC Budget Estimate for Fiscal Year 1993: Hearings Before a Subcomm. of the Comm. on Appropriations*, 102d Cong., 2d Sess. 543, 564 (1992) (same for 1991).

[6] Merrill Lynch & Co., *Mergerstat Review 1991*, at 74-75 (1992).

Bankshares as permitting a claim for lost state remedies based on speculation, not proof of an actual loss, also conflicts with the decisions of other courts of appeals. *See, e.g., Boone v. Carlsbad Bancorporation, Inc.*, 972 F.2d 1545, 1556-59 (10th Cir. 1992). By effectively ruling that an appraisal remedy is presumed to be lost any time it is available but not pursued, the Sixth Circuit is basically relegating *Virginia Bankshares* to the unusual situation where there is no appraisal remedy at all.

Second, the Sixth Circuit's adoption of a lost state remedies theory of causation is inconsistent with the rationale underlying this Court's decision in *Virginia Bankshares* and is unnecessary to the fulfillment of the purpose of the federal proxy laws. Rather than allowing federal securities litigation to turn on speculation, conjecture and inferences about what people "would have thought and done" under circumstances that did not occur—a situation in which "[r]eliable evidence would seldom exist" and resolution would virtually always require trial—this Court chose to adopt a bright line standard for proving causation under which plaintiffs must prove that their minority votes were "legally required" to consummate the transaction. 111 S. Ct. at 2763, 2765 & n.12. The Sixth Circuit's lost state remedies theory depends on exactly the type of "hazy" speculation and conjecture that *Virginia Bankshares* condemned. The Sixth Circuit's theory is also inconsistent with the federal policy underlying the securities laws of protecting the voting rights of shareholders whose votes are needed to approve a corporate action, not facilitating the use of state law remedies for shareholders whose votes are unnecessary. Because this Court did not reach this issue in *Virginia Bankshares*, it remains an important issue left open that has not been, but should be, resolved by this Court.

I. THIS COURT SHOULD GRANT CERTIORARI TO REVIEW THE SIXTH CIRCUIT'S RECOGNITION OF AN IMPLIED PRIVATE RIGHT OF ACTION UNDER SECTION 13(e)(1), WHICH CONFLICTS WITH THE DECISIONS OF THIS AND OTHER FEDERAL COURTS.

A. The Sixth Circuit's Conclusion That Congressional Silence Supports The Implication Of A Private Right Of Action Is Contrary To *Transamerica*, *Touche Ross* And *Virginia Bankshares*.

The Sixth Circuit determination that Section 13(e)(1) gives rise to an implied private action for damages is contrary to the decisions of this Court. The Sixth Circuit grounded its conclusion in its view that Congressional silence *supported* the implication of private actions. *See Howing I*, 826 F.2d at 1474, 1475-76. But *Touche Ross* and *Transamerica* require *affirmative evidence* of Congress' intent to imply private rights of action. In *Touche Ross*, this Court rejected the argument that a private right of action should be inferred whenever Congress does not expressly deny such an action, stating that "implying a private right of action on the basis of congressional silence is a hazardous enterprise, at best." 442 U.S. at 571. At most, Congressional silence "is not inevitably inconsistent with" and "does not automatically undermine" a contention that Congress intended to imply a private right of action; however, silence is "hardly helpful" to that contention. *Transamerica*, 444 U.S. at 18.[7] These holdings were reaffirmed only last Term in *Virginia Bankshares*, where this Court found that Congressional silence was a "serious obstacle" to recognizing a more expansive cause of action under Section 14(a). 111 S. Ct. at 2764.

Transamerica and *Touche Ross* also directed the lower courts not to imply private rights of action when Con-

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[7] *See also Middlesex County Sewerage Auth. v. National Sea Clammers Ass'n*, 453 U.S. 1, 15 (1981) (implied rights will not be found "[i]n the absence of strong indicia of a contrary congressional intent").

gress expressly provided other remedies in the same statute.[8] The Sixth Circuit ignored this principle. It failed to recognize that Congress provided Section 18(a) of the Securities Exchange Act to remedy violations of Section 13(e)(1).[9] *Touche Ross* and other federal court decisions have refused to imply private rights of action under other sections of the Securities Exchange Act by relying on Section 18(a).[10] As recently as *Virginia Bankshares*, this Court found it difficult to "infer[] any congressional urgency to depend on implied private actions to deter violation of § 14(a), when Congress expressly provided private rights of action in §§ 9(c), 16(b) and 18(a) of the same Act." 112 S. Ct. at 2764. The Sixth Circuit's decision finding an implied action violates these well-established principles.

B. This Court's Guidance Is Needed To Resolve The Split Of Authority Between The Courts Of Appeals Regarding The Proper Interpretation Of The Contemporary Legal Context Test Announced In *Cannon*.

The Sixth Circuit's incorrect view of Congressional silence stemmed from its erroneous interpretation of the "contemporary legal context" doctrine this Court an-

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[8] *Transamerica*, 444 U.S. at 19 ("it is an elemental canon of statutory construction that where a statute expressly provides a particular remedy or remedies, a court must be chary of reading others into it"); *Touche Ross*, 442 U.S. at 572 ("when Congress wished to provide a private damages remedy, it knew how to do so and did so expressly").

[9] Section 18(a) allows damages actions against persons filing documents required under the Act which contain "false or misleading" statements. SEC rules require that a proxy statement issued in connection with a going-private merger and the accompanying Schedule 13E-3 be filed with the SEC, thus bringing these documents under the scope of Section 18(a). *See* 17 C.F.R. §§ 240.13e-3(d), 240.14a-6(a), (c); *Kalmanovitz*, 595 F. Supp. at 1394.

[10] *See, e.g., Touche Ross*, 442 U.S. at 571-72; *Liberty National Ins. Holding Co. v. Charter Co.*, 734 F.2d 545, 564-65 (11th Cir. 1984); *Walck v. American Stock Exchange, Inc.*, 687 F.2d 778, 784 (3d Cir. 1982), *cert. denied*, 461 U.S. 942 (1983).

nounced in *Cannon v. University of Chicago*, 441 U.S. 677 (1979). *Cannon* carved out a narrow exception to the general rule disfavoring implied private rights of action in the face of Congressional silence: when Congress explicitly patterns a new statute upon an existing law, and courts had overwhelmingly found a private right of action under that existing law, a court may assume, notwithstanding Congressional silence on the question, that Congress was "thoroughly familiar with these unusually important precedents from this and other federal courts and that [Congress] expected its enactment to be interpreted in conformity with them." 441 U.S. at 699.

The Sixth Circuit's decision far exceeds the narrow exception *Cannon* defined. The Sixth Circuit held that the contemporary legal context embraces the *overall* judicial climate, *i.e.*, how disposed courts were *in general* to find implied private rights of action at the time Congress enacted a statute, rather than just the prior decisions finding an implied action in a law providing the model for the statute in question, as *Cannon* had found. *See Howing I*, 826 F.2d at 1474. Since Section 13(e)(1) was enacted during a fifty-nine year period when the Sixth Circuit viewed implied rights of action as "in a heyday of sorts," [11] the Sixth Circuit reasoned that private remedies could be presumed in the face of Congressional silence. 826 F.2d at 1475.[12]

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[11] From 1916 to 1975, the test in *Texas & Pacific R. Co. v. Rigsby*, 241 U.S. 33 (1916), was used to determine whether private rights of action should be implied. Under *Rigsby*, courts looked only at whether a statute was enacted to benefit a special class, and thus "regarded the denial of a remedy as the exception rather than the rule." *Merrill Lynch, Pierce, Fenner & Smith, Inc. v. Curran*, 456 U.S. 353, 375 (1982); *see also Spicer v. Chicago Board Options Exchange, Inc.*, No. 88-C-2139, 1990 U.S. Dist. LEXIS 14469 at *12 (N.D. Ill. Oct. 24, 1990), (under *Rigsby*, "in the event the statute itself was silent about a private right of action, the Court implied one"), *aff'd*, 1992 Fed. Sec. L. Rep. ¶ 97,016 (7th Cir. 1992). *Rigsby* was overruled by *Cort v. Ash*, 422 U.S. 66, 78 (1975).

[12] The Sixth Circuit at one point attempted to apply a *Cort*-type analysis to the legislative history, only to fall victim to its own mis-

The fallacy of the Sixth Circuit's approach was demonstrated in *Virginia Bankshares*. There, this Court applied the post-1975 analysis for discerning whether to imply a private damages action—*Cort* and *Touche Ross*—to determine whether Congress intended the implied right of action under Section 14(a) to include certain individuals. *Virginia Bankshares*, 111 S. Ct. at 2763-64. But, like Section 13(e), Section 14(a) was also enacted during the pre-*Cort/Touche Ross* era when implied rights of action were "in a heyday of sorts" under *Rigsby*. Under the Sixth Circuit's reasoning, this Court should have applied *Rigsby* rather than *Cort and Touche Ross*. Instead, this Court applied the *current* test for finding implied actions, rather than the outdated and overruled *Rigsby* test. *Id.*

Contrary to *Virginia Bankshares*, the Sixth Circuit's position would effectively overrule this Court's current approach, and reinstate *Rigsby* for all statutes enacted between 1916 and 1975 (*see* note 11, *supra*).[13] Moreover,

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reading of the Congressional record. The court stated that Section 13(e)(1) was patterned after Section 14(a), 826 F.2d at 1475, which this Court held gave rise to a private right of action in *J. I. Case Co. v. Borak*, 377 U.S. 426 (1964). But the Sixth Circuit's statement was based on a comment of Senator Williams that referred to the tender offer provisions of the Williams Act, ultimately codified at Section 14(e), not the going-private provisions codified in Section 13(e)(1). In fact, as Senator Williams made clear, Section 13(e)(1) was "based on language in section 15(c)(2)" of the Act. 114 Cong. Rec. 21,954 (1968) (remarks of Sen. Williams). And there is no implied damages action under Section 15(c). *See, e.g., Brannan v. Eisenstein*, 804 F.2d 1041, 1043 n.1 (8th Cir. 1986); *Western Federal Corp. v. Erickson*, 739 F.2d 1439, 1444 n.5 (9th Cir. 1984).

[13] Many of these statutes have already come under the scrutiny of this Court in decisions that do not evince any special willingness to find private actions based on the date when the statute was enacted. *See, e.g., Massachusetts Mutual Life Ins. Co. v. Russell*, 473 U.S. 134 (1985) (no implied cause of action under Section 409(a) of Employee Retirement Income Security Act of 1974); *Middlesex County Sewerage Auth. v. National Sea Clammers Ass'n*, 453 U.S. 1 (1981) (no implied cause of action under Federal Water Pollution Control Act of 1948 or Marine Protection, Research &

under this theory, each time this Court alters its approach to implying private rights of action, the lower courts will only employ that analysis prospectively because the previous tests were part of the "contemporary legal context" under which earlier statutes were enacted. There is nothing in *Cannon* or any other decision of this Court which suggests such a drastic result.

Other courts of appeals have rejected this version of the contemporary legal context theory. In *Siebert v. Conservative Party*, 724 F.2d 334, 337 (2d Cir. 1983), *cert. denied*, 466 U.S. 980 (1984), the Second Circuit refused to distort *Cannon* into a rule "that the law must be frozen in time for purposes of determining whether Congress intended an implied right of action to exist." Instead, the Second Circuit held that *Cannon*

> merely restate[s] the canon of statutory construction that Congress is presumed to be aware of the judicial background against which it legislates. *A lower federal court, however, must employ the analysis currently required by the Supreme Court for making the determination of Congressional intent.*

Id. (emphasis supplied).[14]

Sanctuaries Act of 1972); *Northwest Airlines, Inc. v. Transport Workers Union*, 451 U.S. 77 (1981) (no implied cause of action for contribution under Equal Pay Act of 1963 or Title VII of Civil Rights Act of 1964); *Universities Research Ass'n v. Coutu*, 450 U.S. 754 (1981) (no implied cause of action under Section 1(a) of Davis-Bacon Act of 1931); *Kissinger v. Reporters Committee*, 445 U.S. 136, 147-50 (1980) (no implied cause of action under Federal Records Disposal Act of 1968).

[14] The Second Circuit has repeatedly adhered to its rejection of the Sixth Circuit's analysis. In *Reeves v. Continental Equities Corp. of America*, 912 F.2d 37, 40-41 (2d Cir. 1990), the Second Circuit declared: "Regardless of the law at the time of enactment of the [statute]. . . . the court must determine whether a private cause of action is implied on the basis of the *Cort v. Ash* factors." The Second Circuit recently reaffirmed its view that *Cannon* and other decisions require a court "to determine whether a private cause of action is implied by applying the law in effect at the time of decision . . . rather than the method of analysis that courts applied

The Third Circuit has also rejected this theory. In *American Tel. & Tel. Co. v. M/V Cape Fear*, 967 F.2d 864, 871-72 (3d Cir. 1992), the court recognized that the Supreme Court applies only the *current* test to find private rights of action:

> As *Cort v. Ash* and many succeeding cases demonstrate, however, the Supreme Court has consistently applied contemporary implication precepts to statutes enacted at a time when implication was the rule rather than the exception. . . . We are bound by the rules of implication set forth in and after *Cort v. Ash*, and may not decide this case on our view of "what Congress probably assumed" when it passed the [statute].

This Court should grant certiorari to reaffirm that the contemporary legal context test is as narrow as the Second and Third Circuits have held, not the license to ignore *Cort*, *Transamerica* and *Touche Ross* that the Sixth Circuit would have it be.

C. This Court's Guidance Is Needed To Resolve The Split Of Authority Between Federal Courts Regarding Whether An Implied Private Right Of Action Exists Under Section 13(e)(1).

The lower federal courts are in conflict regarding whether an implied right of action for damages exists under Section 13(e)(1). Unlike the Sixth Circuit,[15] two courts have refused to imply such actions after careful consideration of *Transamerica* and *Touche Ross*. In addition, Judge Guy, who joined in the Sixth Circuit's original opinion finding a private right of action, has "since had second thoughts and now ha[s] serious doubts about that conclusion." *Howing III*, 972 F.2d at 711 n.1.

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at the time of a statute's enactment." *Health Care Plan, Inc. v. AETNA Life Ins. Co.*, 966 F.2d 738, 742 (2d Cir. 1992).

[15] Besides the Sixth Circuit, two other courts have found a private right of action for money damages under Section 13(e)(1). *See Fisher v. Plessey Co.*, 1982-83 Fed. Sec. L. Rep. (CCH) ¶ 99,246 at 96,073 (S.D.N.Y. 1983); *Dowling v. Narragansett Capital Corp.*, 735 F. Supp. 1105, 1116 (D.R.I. 1990).

In *Kalmanovitz v. G. Heileman Brewing Co.*, 595 F. Supp. 1385, 1394-95 (D. Del. 1984), *aff'd*, 769 F.2d 152 (3d Cir. 1985), the court followed *Transamerica* and *Touche Ross* in ruling that no implied private damages action exists under Section 13(e). The *Kalmanovitz* court concluded that "in light of the recent Supreme Court decisions which refuse to imply a private right of action for damages," and "[b]ecause the legislative history of the 1934 Exchange Act is silent on the issue of whether a private cause of action for damages should be available under Section 13(e), . . . no private right of action for money damages exists under Section 13(e)." *Id.* at 1395.[16]

Similarly, the court in *Berg v. First American Bankshares, Inc.*, 1984-85 Fed. Sec. L. Rep. (CCH) ¶ 92,011 at 91,012 (D.D.C. 1985), *aff'd*, 796 F.2d 498 (D.C. Cir. 1986), also relied on *Transamerica* and *Touche Ross* to find that "no private damages remedy should be implied if the language of the statute and legislative history are silent, particularly if the statute contains other sections which include provisions for enforcement and remedies." Because "[n]either the language nor the legislative history of Section 13(e) expressly or implicitly provides a private damages remedy," and given the applicability of Section 18(a) to Section 13(e) violations, the court declined to imply a private right of action. *Id.* at 91,013.

This Court should grant certiorari to resolve this conflict, to provide guidance to the lower federal courts on the scope of *Cannon*, and to reaffirm *Transamerica* and *Touche Ross*. The Sixth Circuit's decision to create a private right of action under Section 13(e)(1) has great significance to the national securities markets, particularly in view of the number of going-private mergers, and the amount of commerce involved. *See* p. 9, *supra*.

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[16] The Sixth Circuit erroneously distinguished *Kalmanovitz* by claiming that Section 18(a) did not provide relief for violations of Section 13(e). *Howing I*, 826 F.2d at 1476 n.4. However, as discussed at note 9, *supra*, it is the Sixth Circuit that has incorrectly interpreted the applicability of Section 18(a) to Section 13(e).

Moreover, the split between the Sixth Circuit's view of the contemporary legal context test and the application and interpretation of that test in *Virginia Bankshares* and the lower federal courts has even broader implications for the creation of other actions under numerous other statutes.[17]

II. THIS COURT SHOULD GRANT CERTIORARI TO REVIEW THE SIXTH CIRCUIT'S PRESUMPTION OF MATERIALITY, WHICH CONFLICTS WITH DECISIONS OF BOTH THIS COURT AND THE FEDERAL COURTS OF APPEALS.

A. The Sixth Circuit's Decision On Materiality Conflicts With This Court's Decisions In *TSC*, *Basic* And *Virginia Bankshares*.

In *TSC Indus., Inc. v. Northway, Inc.*, 426 U.S. 438 (1976), this Court announced the standard for determining materiality under the federal securities laws. In considering a claim under Section 14(a) of the Securities Exchange Act, the Court required plaintiffs to establish "a substantial likelihood that, under all the circumstances, the omitted fact would have assumed actual significance in the deliberations of the reasonable shareholder." *Id.* at 449. Under that standard, information that does not alter the " 'total mix' of information made available" is immaterial and does not give rise to liability. *Id.* at 448, 449. The determination is made not by looking at the information in the abstract, but rather by scrutinizing the information in the context of "all the circumstances" of the pending transaction. *Id.* at 449.

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[17] The Sixth Circuit has also attempted to circumvent the federal prohibition against implying actions in the face of Congressional silence by concluding that a violation of Section 13(e) by Nationwide Corp. gives rise to a *state* law cause of action against Nationwide Mutual. The Sixth Circuit acknowledges that plaintiffs' sole remaining claim is the same, whether stated under federal or state law. *Howing II*, 927 F.2d at 269. Yet, as Judge Guy notes in dissent, the Sixth Circuit has created a state law cause of action based on a violation of federal law without finding any real support in Ohio law. *See Howing III*, 972 F.2d at 712. This Court cannot permit the Sixth Circuit to so avoid this Court's precedents.

The Sixth Circuit's presumption of materiality is fundamentally inconsistent with the *TSC* materiality standard. Ignoring this Court's clear precedent, the Sixth Circuit held that the language of an SEC instruction arguably directing a discussion of book, liquidation and going concern value "creates in effect a presumption" that any omitted facts concerning those valuations would be material whatever the "circumstances" and regardless of the "total mix of information made available." *See Howing II*, 927 F.2d at 265. Such a rule, making the inclusion of an item in an SEC regulation or schedule the presumptive determinant of materiality regardless of the circumstances of the transaction, could impose liability on account of misstatements or omissions of trivial information, a result against which *TSC* cautioned.

Ironically, the Sixth Circuit justified what it called a "heightened" standard on a ground specifically rejected by this Court in reversing another Sixth Circuit decision. This Court reversed the Sixth Circuit in *Basic Inc. v. Levinson*, 485 U.S. 224 (1988), rejecting the use of a different standard of materiality in cases such as going-private mergers where insiders allegedly have greater access to information. *Id.* at 240 n.18. In *Basic*, this Court disapproved of the Sixth Circuit's mechanical disclosure test for merger discussions because it failed to properly recognize the element of materiality. *Id.* at 237-38. This Court reiterated that materiality is a "fact-specific inquiry" which "depends on the significance the reasonable investor would place on the withheld or misrepresented information." *Id.* at 240. The Court refused to endorse a different standard of materiality in cases involving what the Sixth Circuit now refers to as "coercive" transactions—*i.e.*, where insiders are involved:

> Devising two different standards of materiality, one for situations where insiders have traded in abrogation of their duty to disclose or abstain (or for that matter when any disclosure duty has been breached) and another covering affirmative misrepresentations by those under no duty to disclose (but under the ever-

> present duty not to mislead), would effectively collapse the materiality requirement into the analysis of defendant's disclosure duties.

Id. at 240 n.18.

The Sixth Circuit's new presumption of materiality causes the same collapse of materiality and disclosure that this Court rejected in *Basic*. Under a "presumption" standard, materiality is presumed any time there is a duty to disclose, effectively eliminating materiality as a discrete element of a claim for relief. This equating of disclosure duty and materiality is contrary to *TSC* and *Basic*, because it renders any omission of information covered by a disclosure requirement, no matter how trivial, *per se* material.

The Sixth Circuit's reasoning also conflicts with *Virginia Bankshares*, this Court's most recent materiality decision. In *Virginia Bankshares*, this Court applied the *TSC* standard in a case involving the same kind of transaction as the Sixth Circuit said required a "heightened" standard in evaluating a proxy statement used in a going-private or "freeze-out" merger. *See Virginia Bankshares*, 111 S. Ct. at 2756; *Howing II*, 927 F.2d at 264. This Court declared that liability under the securities laws "must rest not only on deceptiveness but materiality as well (*i.e.*, it has to be significant enough to be important to a reasonable investor deciding how to vote, *see TSC Indus.*, 426 U.S. at 449)." 111 S. Ct. at 2760.

Thus, *Virginia Bankshares*, like this Court's earlier decision in *Basic*, rejected the Sixth Circuit's position that a different standard or burden of proof should apply in judging materiality in going-private or "freeze-out" mergers. *Virginia Bankshares* establishes that the *TSC* burden of proof, and not the "presumption" of materiality employed by the Sixth Circuit, should be applied in going-private merger cases. Under *Virginia Bankshares*, plaintiffs cannot circumvent their burden of proving materiality under *TSC* by relying on a "presumption."

B. This Court's Guidance Is Needed To Resolve The Split Between The Sixth Circuit And Other Circuits Concerning The Proper Standard Of Materiality.

The Sixth Circuit's decision also conflicts with at least three lines of decisions by the federal courts of appeals. *First*, every other court of appeals has applied the *TSC* standard to *all* provisions of the federal securities laws,[18] and the Sixth Circuit's decision that the *TSC* standard does not control cases arising under Section 13(e)(1) of the Securities Exchange Act is directly contrary to *Berg v. First American Bankshares, Inc.*, 796 F.2d 489 (D.C. Cir. 1986), where the D.C. Circuit held that the *TSC* materiality standard governs Section 13(e)(1) cases. The *Berg* court held that "[l]iability under Section 13(e)(1) and Rule 13e-3 promulgated thereunder requires that any misrepresentation or omission be material." It went on to find that its "conclusion that any defects in the proxy statement were immaterial for purposes of liability under sections 10(b) and 14(a)"—a determination based on application of the *TSC* standard—"applie[d] equally to Section 13(e)." *Id.* at 495, 502. Thus, the D.C. Circuit recognized that there was no liability under Section 13(e) and Rule 13e-3 without a finding of materiality under the *TSC* standard.

Second, the Sixth Circuit's belief that a different materiality standard is appropriate in cases involving omission of information required by an SEC regulation is contrary to other leading appellate authority applying *TSC* in those contexts. The Sixth Circuit's decision is contrary to the Second Circuit's analysis of an alleged failure to disclose information required by Schedule 13D, another SEC form published in an SEC regulation. In *United States v. Bilzerian*, 926 F.2d 1285, 1298 (2d Cir.), *cert. denied*, 112 S. Ct. 63 (1991), the Second Circuit held that infor-

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[18] *Flamm v. Eberstadt*, 814 F.2d 1169, 1174 (7th Cir.) ("like *every other court of appeals* we have taken the definition in *TSC* as suitable for the term [materiality] wherever it appears in securities law") (emphasis supplied), *cert. denied*, 484 U.S. 853 (1987).

mation required to be disclosed in Schedule 13D is *not* presumptively material; "[t]he standard of materiality under the securities law was set forth by the Supreme Court in *TSC*." In analyzing defendant's Schedule 13D omissions, the Second Circuit "decline[d] to hold that the information required to be disclosed in 13D is material *per se*," even if "such disclosure is required under the securities laws." *Id. See also Levine v. NL Indus., Inc.*, 926 F.2d 199, 202-03 (2d Cir. 1991) (applying *TSC* in finding that a failure to disclose an item mandated by SEC regulation in Form 10-K filings was not actionable since it was not material).

Similarly, in *Flaxman v. Commodity Futures Trading Comm'n*, 697 F.2d 782, 786 (7th Cir. 1983), the Seventh Circuit applied *TSC* to omissions of information specifically requested by an SEC application and cautioned that not all "information requested by the Commission is necessarily material." [19] These cases properly recognize that the items included on SEC schedules are a listing of everything the SEC has deemed in advance *could* be material. But there may be items which are arguably required to be disclosed that, in the context of a specific transaction, are not important to a reasonable shareholder.[20]

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[19] *See also MAI Basic Four, Inc. v. Prime Computer, Inc.*, 871 F.2d 212, 221-22 (1st Cir. 1989) (liability for failure to furnish all items of information required for compliance with Schedule 14D-1 was predicated on whether the information required was material under *TSC*); *Susquehanna Corp. v. Pan American Sulphur Co.*, 423 F.2d 1075, 1085 (5th Cir. 1970) (party filing Schedule 13D liable only for failure to disclose "*material* facts called for by the various items of the schedule") (emphasis supplied).

[20] Item 8(b) of Schedule 13E-3—the provision on which the Sixth Circuit relied as the basis for its presumption—acknowledges this by stating that the issuer should discuss "in reasonable detail *the material factors* upon which the belief stated in Item 8(a) is based and, to the extent practicable, the weight assigned to each such factor." 17 C.F.R. § 240.13e-100, Item 8(b) (1990) (emphasis supplied). As the SEC has observed, these factors "need be discussed only to the extent that they are material in the context of the

Third, the Sixth Circuit's belief that a different materiality standard is warranted in cases where management or other insiders are responsible for making the allegedly faulty disclosure, including cases involving going-private mergers, conflicts with decisions of other federal appeals courts applying *TSC* to cases involving such transactions. In *Pavlidis v. New England Patriots Football Club, Inc.*, 737 F.2d 1227, 1231 (1st Cir. 1984), the First Circuit held that "[t]he fact that a proxy statement is drafted by insiders acting in their own interests *does not change the standard of materiality.*" (Emphasis supplied.) In *Cole v. Schenley Indus., Inc.*, 563 F.2d 35, 40 n.9 (2d Cir. 1977), the Second Circuit declined appellant's invitation "to apply a different legal standard of materiality to proxy statements involving mergers," and applied the *TSC* standard. In *Michaels v. Michaels*, 767 F.2d 1185, 1196-97 (7th Cir. 1985), *cert. denied*, 474 U.S. 1057 (1986), the Seventh Circuit rejected an argument that "a more subjective standard of materiality applies when the corporation is closely-held" and applied *TSC*.[21] As these authorities show, nothing about going-private mergers requires a different standard of materiality.

This Court's attention and guidance are needed to resolve these conflicting views as to the proper standard of materiality under the securities laws, specifically under Section 13(e)(1). As discussed at pp. 8-9, *supra*, resolution of this issue is of significant importance in light of the thousands of securities cases filed and the hundreds of going-private transactions regulated each year. This

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transaction." Sec. Ex. Act Rel. 17,719, 22 SEC Dock. 783, 798 (1981).

[21] *See also Santa Fe Indus., Inc. v. Green*, 430 U.S. 462, 474 n.14 (1977) (*TSC* standard applied to merger transaction used by majority stockholder to eliminate the minority interest); *Landy v. Amsterdam*, 815 F.2d 925, 932 (3d Cir. 1987) (minority shareholders' challenge to merger analyzed under *TSC*); *Lockspeiser v. Western Maryland Co.*, 768 F.2d 558, 561 (4th Cir. 1985) (minority shareholder's challenge to corporation's merger with subsidiary analyzed under *TSC*).

Court should announce a uniform national rule for treatment of such transactions under the securities laws.[22]

III. THIS COURT SHOULD GRANT CERTIORARI TO REVIEW THE SIXTH CIRCUIT'S DETERMINATION THAT A SHAREHOLDER CAN ESTABLISH CAUSATION BY PROOF OF LOST STATE REMEDIES, THE QUESTION LEFT OPEN IN *VIRGINIA BANKSHARES*.

A. The Sixth Circuit's Decision On Causation Is Contrary To The Analysis Mandated In *Virginia Bankshares* That Causation Cannot Be Established Where There Is No Indication That The Proxy Solicitation Resulted In Lost State Remedies.

In *Virginia Bankshares*, the Supreme Court left open the question of whether a shareholder can meet the required element of causation by showing that errors or omissions in a proxy statement resulted in lost state remedies. 111 S. Ct. at 2766. In doing so, this Court refused to allow lower courts to establish a lost state remedies causation theory where there is "no indication in the law or facts" that a "proxy solicitation resulted in any such loss." *Id.* Because the record showed no loss of state remedies, the Court held that the requisite causation was lacking. *Id.*

Here, the Sixth Circuit engaged in the very analysis forbidden by *Virginia Bankshares*: establishing a lost state remedies causation theory without any indication that the proxy solicitation resulted in a lost state remedy. In this case, the uncontradicted evidence shows that plaintiffs were not "duped" into forfeiting their appraisal rights under state law. *See Howing III*, 972 F.2d at 711;

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[22] Once again, since only an omission that is "material" under *TSC* can constitute a violation of Section 13(e), the Sixth Circuit's creation of an Ohio claim for violation of Section 13 cannot stand in light of the District Court's finding of immateriality under *TSC*. *See Howing II*, 927 F.2d at 269 (state claim comprised solely of "the omission of this same information (required by Rule 13e-3)" and "proof of material omissions . . . will be similar under either theory").

SA 641. Plaintiffs were fully informed of their appraisal rights and provided with potential reasons for exercising those rights. (JA 93, 97-98.) They refrained from voting on the merger (JA 246), thereby preserving their ability to pursue an appraisal. *See* Ohio Rev. Code Ann. § 1701.85. As plaintiffs and their counsel admitted and the District Court found, plaintiffs were fully capable of exercising their appraisal rights, but they consciously elected not to pursue those rights. (SA 623, 627-28, 630-31, 633-36, 641.)

As Judge Guy noted in dissent, it is clear that there was no "forfeiture of the appraisal remedy." *Howing III*, 972 F.2d at 711. The Sixth Circuit panel majority never questioned or disturbed the District Court's finding that plaintiffs "could have" but "have chosen" not to pursue their appraisal remedy. (SA 641.) Instead, the panel speculated, disregarding the evidence and the District Court's finding, that "plaintiffs' decisions with respect to appraisal might well have been different" had some additional disclosure been made. Such speculation, the panel held, was enough for the plaintiffs to establish "causation supportive of their § 13(e) claim." *Id.* at 710.

The Sixth Circuit's decision conflicts with *Virginia Bankshares*' holding that causation is lacking where "there is no indication in the law or facts" that the proxy solicitation resulted in lost state remedies. 111 S. Ct. at 2766. By substituting its own speculation that plaintiffs *might* have lost a state law appraisal remedy for uncontradicted evidence showing that plaintiffs knowingly elected not to pursue that remedy, the Sixth Circuit wrongly departed from *Virginia Bankshares*. Indeed, because the Sixth Circuit's approach *presumes* that plaintiffs would "lose" whatever state law appraisal rights are available, and because those rights are available for nearly every merger transaction, the panel's decision effectively enables nearly every plaintiff to establish causation without having to come forward with proof of an actual loss. This will open up the federal courts to serve

as a forum for plaintiffs to pursue a *federal* claim based on *state* appraisal rights, except in those rare situations where appraisal rights do not exist. Thus, the Sixth Circuit essentially reads *Virginia Bankshares* as applying only to mergers involving banks in Virginia, for which no appraisal remedy is provided. 111 S. Ct. at 2766 n.14.

The Sixth Circuit's decision also conflicts with decisions of other federal courts of appeals that have correctly applied *Virginia Bankshares* to bar speculative claims of lost state remedies for lack of causation. In *Boone v. Carlsbad Bancorporation, Inc.*, 972 F.2d 1545, 1558 & n.11 (10th Cir. 1992), the Court of Appeals held that causation could not be established by plaintiffs' assertions that they "*might* have been very *interested* in trying to stop" the merger by seeking a state court injunction and that "[h]ad I had information, I possibly would have done something." (Emphasis in original.) The Tenth Circuit ruled that it would be "mere speculation to assume that plaintiffs *would* have sought an injunction." *Id.* at 1559 (emphasis in original). Correctly applying *Virginia Bankshares*, the Tenth Circuit affirmed summary judgment against plaintiffs because they failed to present "evidentiary materials sufficient to establish a factual issue on causation stemming from an allegedly lost state remedy." *Id.* at 1558.

Similarly, in *Scattergood v. Perelman*, 945 F.2d 618 (3d Cir. 1991), the Court of Appeals ruled that no claim for loss of state remedies can be maintained under the federal securities laws without proof that the remedy was in fact lost. The Third Circuit held that the causation required by *Virginia Bankshares* was lacking because plaintiffs could not establish that they lost "an opportunity under state law to enjoin a merger." *Id.* at 626 n.4.[23]

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[23] In *Wilson v. Great American Indus., Inc.*, 979 F.2d 924, 931 (2d Cir. 1992), the Second Circuit ruled that a plaintiff may establish causation by proof of lost state remedies. But it emphasized that the theory must be proven with evidence, not assumed based

This Court should grant certiorari to reverse the Sixth Circuit's departure from *Virginia Bankshares'* holding that there can be no federal claim for a lost state remedy without proof that the proxy solicitation caused the loss, and that mere speculation about such a loss will not suffice.[24]

B. The Sixth Circuit's Decision Permitting A Cause Of Action For Lost State Remedies Is Inconsistent With This Court's Precedents And Federal Policy.

Having speculated that plaintiffs had lost a state law remedy of an appraisal, the Sixth Circuit's panel majority went on to decide the question left open in Virginia *Bankshares*: whether the federal securities laws provide a cause of action for lost state remedies. 111 S. Ct. at 2766.[25] The panel answered the question affirmatively. That answer is not only wrong, but the rationale on which it is based is inconsistent with this Court's securities law precedents and applicable federal policy.

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on speculation. *Id.* at 932 (remanding for "purpose of determining whether the proxy solicitation actually resulted in the loss of any remedies available to plaintiffs under New York law").

[24] The Sixth Circuit cannot be allowed to avoid *Virginia Bankshares'* holding on causation by permitting plaintiffs to maintain their federal disclosure claim under the guise of state law. Causation is lacking not only because plaintiffs' votes were not required to authorize the going-private merger, *Virginia Bankshares*, 111 S. Ct. at 2761-63, but also because Ohio law does not require a proxy statement or require disclosure of the information specified in Item 8(b) of SEC Schedule 13E-3. *Klein v. Fisher Foods, Inc.*, 216 N.E.2d 647, 656 (Ohio 1965).

[25] This Court's reluctance to reach the "lost state remedies" issue in *Virginia Bankshares* does not indicate an acceptance of the theory, only adherence to the Court's practice of disposing of cases on the narrowest possible grounds. *See, e.g., Ashwander v. Tennessee Valley Auth.*, 297 U.S. 288, 347 (1936) (Court should only reach issues absolutely necessary to its decision). Following *Virginia Bankshares*, the Tenth Circuit left the same question open in *Boone v. Carlsbad Bancorporation, Inc.*, 972 F.2d at 1558 n.12 ("we need not reach the question, also reserved in *Virginia Bankshares*, whether a cause of action for lost state remedies lies here").

As this Court noted in *Virginia Bankshares*, claims based on what the plaintiffs or defendants might have done if the proxy statement was not misleading would turn on " 'hazy' issues inviting self-serving testimony, strike suits, and protracted discovery." 111 S. Ct. at 2765. The plaintiffs in *Virginia Bankshares* tried to establish an alternative causation theory by speculating that the parties *might* have refused to consummate the merger in the absence of approval by the minority stockholders. This Court rejected the argument. The Court refused to allow federal securities litigation to turn on speculation, conjecture and "inferences about what the corporate directors would have thought and done without the minority shareholder approval unneeded to authorize action"—a situation in which "[r]eliable evidence would seldom exist" and resolution would virtually always require trial. *Id.* at 2765 & n.12. Instead, the Court adopted a bright line standard under which plaintiffs must prove that the minority stockholders' votes were "legally required" to consummate the transaction. *Id.* at 2763.

This Court should adhere to the *Virginia Bankshares* standard and preclude plaintiffs who cannot otherwise prove causation from alleging that they would have availed themselves of a state law remedy without the proxy violation. If plaintiffs were permitted to assert this lost state remedy theory whenever they are otherwise unable to establish causation, all cases would become mired in the very speculative and hazy issues this Court cautioned against in *Virginia Bankshares*.[26]

The Sixth Circuit justified adoption of its version of the lost state remedy theory based on this Court's analysis in *Mills v. Electric Auto-Lite Co.*, 396 U.S. 375, 385 n.7 (1970). But the whole rationale for a relaxed causation standard in *Mills* was that where the votes

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[26] In addition, summary judgment could always be avoided based on plaintiff's mere self-serving assertions that they would have exercised theoretical state law remedies, a concern this Court has previously invoked. *See Blue Chip Stamps v. Manor Drug Stores*, 421 U.S. 723, 740-42 (1975).

sought *were* needed to consummate the transaction, the proxy statement could fairly be considered an "essential link." Where, as here, and as in *Virginia Bankshares*, the votes are *not* needed to consummate the merger, the proxy statement is not such an "essential link." [27]

The Sixth Circuit's lost state remedy theory is also at odds with the policy underlying the federal securities laws that pertain to proxy statements. The purpose of the federal proxy laws is "to prevent management or others from *obtaining authorization for corporate action* by means of deceptive or inadequate disclosure in proxy solicitation." *J.I. Case Co. v. Borak*, 377 U.S. 426, 431 (1964) (emphasis supplied). The federal policy is thus intended to protect the voting process for shareholders whose votes *are needed* to approve corporate action, not to facilitate the use of state law remedies for shareholders whose votes are unnecessary. Contrary to that federal purpose, the lost state remedy theory would permit shareholders whose voting rights are unaffected to recover damages in federal court for allegedly missing out on potential state law claims. The creation of such a remedy under the federal securities laws is improper. As this Court has ruled, no cause of action should be "implied where it is 'unnecessary to ensure the fulfillment of Congress' purposes' in adopting the [Securities Exchange] Act." *Santa Fe Indus., Inc. v. Green*, 430 U.S. 462, 477 (1977) (quoting *Piper v. Chris-Craft Indus.*, 430 U.S. 1, 41 (1977)).

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[27] The Sixth Circuit erroneously stated that three current Justices of this Court have "accepted the loss-of-state-law-remedy theory of causation." *Howing III*, 972 F.2d at 705 n.4. In fact, these Justices have merely criticized the majority opinion in *Virginia Bankshares* for not resolving the issue. *See* 111 S. Ct. at 2773 (Kennedy, J., dissenting) (stating that Court should not avoid the question). The Sixth Circuit also stated that its lost state remedies causation theory was supported by Congressional intent "that an implied private right of action arise under § 13(e)." 972 F.2d at 708. But, as discussed in Part I.A, *supra*, Congress expressed no such intent in enacting Section 13(e).

This Court's resolution of the lost state remedies question is also needed to eliminate the confusion in the Circuit Courts about the proper interpretation of *Virginia Bankshares*' holding on causation. The D.C. Circuit has read *Virginia Bankshares* as barring any private right of action for "minority shareholders who lacked the votes needed to block the merger that gave rise to the claim." *Roosevelt v. E.I. DuPont de Nemours & Co.*, 958 F.2d 416, 420 (D.C. Cir. 1992). The Sixth Circuit has staked out an exception to that bar in adopting the lost state remedy theory.

This Court should grant certiorari to address the lost state remedies theory of causation expressly left open in *Virginia Bankshares*.

CONCLUSION

For the foregoing reasons, a writ of certiorari should issue to review the judgments and opinions of the Sixth Circuit in this case.

Respectfully submitted,

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Dated: February 2, 1993

APPENDIX

APPENDIX

UNITED STATES COURT OF APPEALS
FOR THE SIXTH CIRCUIT

No. 89-4084

HOWING COMPANY; DOUGLAS MCLELLAN,
Plaintiffs-Appellants,

v.

NATIONWIDE CORPORATION;
NATIONWIDE MUTUAL INSURANCE COMPANY,
Defendants-Appellees,

On Appeal from the United States District Court
for the Southern District of Ohio

Decided and Filed August 17, 1992

Before: MERRITT, Chief Judge; GUY, Circuit Judge; and BROWN, Senior Circuit Judge.

BROWN, Senior Circuit Judge, delivered the opinion of the court, in which MERRITT, Chief Judge, joined. GUY, Circuit Judge (pp. 22-25), delivered a separate dissenting opinion.

BAILEY BROWN, Senior Circuit Judge. This securities action brought by minority public shareholders of Nationwide Corporation arises from a freeze-out merger of Nationwide Corporation with a parent corporation, Nationwide Mutual Insurance Company, which, with another parent, Nationwide Mutual Fire Insurance Company, immediately prior to the merger owned approximately 85% of the shares of the subsidiary. We previously reversed the district court's dismissal of the mi-

nority shareholders' claims that the Defendants issued a proxy statement that violated SEC Rule 13e-3 and breached their state-law fiduciary duties to the minority shareholders. We then remanded the case for further proceedings consistent with out opinion. *See Howing Co. v. Nationwide Corp.*, 826 F.2d 1470 (6th Cir. 1987).

Upon remand, concluding that the omitted Rule 13e-3 disclosures were not material and that the Defendants did not breach state-law fiduciary duties, the district court again granted summary judgment for the Defendants. The minority shareholders again appealed to this court, and we again reversed and remanded. We concluded that the nondisclosures were presumptively material and that the minority shareholders had supported a state-law breach-of-fiduciary-duty claim. *See Howing v. Nationwide*, 927 F.2d 263 (6th Cir. 1991).

The Supreme Court then granted the Defendants' application for certiorari. The Court vacated the judgment of this court and remanded for reconsideration in light of its intervening decision in *Virginia Bankshares, Inc. v. Sandberg*, 501 U.S. ——, 112 S. Ct. 39, 115 L.Ed.2d 929 (1991). For the reasons that follow, we again reverse the judgment of the district court and remand for further proceedings consistent with this opinion.

I.

Nationwide Corporation, a large life insurance holding company, had two classes of outstanding stock. Until the late 1970's, the public held the Class A common stock. Two Nationwide parent companies, Nationwide Mutual Fire Insurance Company ("Nationwide Fire") and Nationwide Mutual Insurance Company ("Nationwide Mutual"), held all of the Class B common stock.

A. The Underlying Facts

The two classes of stock shared voting rights in such a way that complete ownership of Class B gave Nation-

wide Mutual and Nationwide Fire effective control of Nationwide Corporation. During December of 1978, Nationwide Mutual and Nationwide Fire began to eliminate public ownership of Nationwide Corporation. They made a tender offer to buy and bought some of the Class A shares for $20 per share net in cash. After the tender offer, they continued to purchase Class A shares in the open market, at prices ranging from $22.50 to $24.62 per share. Nationwide Mutual and Nationwide Fire thereby acquired ownership of 85.6% of the Class A stock.

During November of 1982, Nationwide Corporation's board of directors approved a freeze-out transaction in which Nationwide Mutual and Nationwide Fire would acquire the remaining Class A shares for $42.50 per share. Because its parents owned over eighty-five percent of its stock, and shareholder approval required the favorable vote of only a majority, the outcome of the shareholder vote was a foregone conclusion. The transaction, which eliminated all public ownership of Nationwide Corporation, was approved by the favorable vote of 94.7% of the Class A shares.[1]

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[1] Near the time of the announcement of the merger, November 19, 1982, Nationwide Corporation had 4,777,437 Class A shares outstanding. Nationwide Mutual owned or controlled 4,091,892 shares, or about 85.6% of the total. Approximately 4,000 public shareholders of record owned the remaining 685,545 shares, which constituted about 14.4% of the total outstanding.

The merger was approved by the favorable vote of 94.7% of the Class A shares, or approximately 4,524,233 shares. The deduction of the 4,091,892 shares owned or controlled by Nationwide Mutual, which obviously were voted in favor of the merger, indicates that approximately 432,341 of the shares held by the 4,000 public shareholders were voted in favor of the merger. The remaining 253,304 shares held by the 4,000 public shareholders were voted against the merger or were not voted. The 1,361 shares held by the Howing Company and the 2,324 shares held by McLellan were among the shares that were not voted.

B. The Ensuing Litigation

Prior to the vote on the proposed merger, Belle Efros, a Nationwide Corporation shareholder, sought a preliminary injunction barring the vote. Following denial of the injunction and the shareholders' approval of the merger, two former Nationwide Corporation shareholders, the Howing Company and Douglas McLellan, brought this action. The district court denied class certification in the *Efros* action. It later, however, conditionally certified the *Howing-McLellan* action as a class action and consolidated it with the *Efros* action. The class certified included all holders of Class A stock except Nationwide Mutual and those it controlled.

The final amended complaint stated claims under, *inter alia*, § 13(e) of the Securities Exchange Act of 1934 and under state law based upon a breach of fiduciary duty. During the November, 1982 freeze-out transaction, Nationwide Corporation had issued a proxy solicitation. When the Nationwide Defendants later sought summary judgment, the district court identified the proxy solicitation's compliance with Rule 13e-3 as the principal issue in this case. It held that the proxy solicitation satisfied Rule 13e-3 and that any omissions were not material.

Additionally, the district court rejected the Plaintiffs' state-law claims. It held that statutory appraisal constituted the Plaintiffs' exclusive state-law remedy. Noting the Plaintiffs' failure even to assert the appraisal remedy, the district court dismissed the complaint.

1. *Howing I*: The First Appeal to the Sixth Circuit

The class Plaintiffs, but not Belle Efros, appealed. We reversed the judgment of the district court and remanded the case. *See Howing Co. v. Nationwide Corp.*, 826 F.2d 1470 (6th Cir. 1987) (hereinafter "*Howing I*").

We first held that a private right of action for damages exists under § 13(e) of the Securities Exchange Act of 1934. We next discussed compliance with Rule

13e-3, 17 C.F.R. § 240.13e-3, a rule, promulgated under § 13(e), that prescribes the form and content of the disclosures that must be given to shareholders in going-private transactions such as the one under consideration. Rule 13e-3 mandates that certain parts of the issuer's Schedule 13E-3, a document that must be filed with the SEC during going-private transactions, be disclosed verbatim in the proxy solicitation.

The instructions to Item 8 of Schedule 13E-3, 17 C.F.R. § 240.13e-100, require a statement as to the fairness of the transaction and the factors upon which such belief is based. In considering the Defendants' compliance with Rule 13e-3, we first noted that conclusory statements that the transaction is fair in relation to net book value, going-concern value, and future prospects fail to satisfy the Rule. Noting that the Rule requires a high level of specificity, we concluded that the Nationwide Defendants had made just the sort of conclusory statements prohibited by the Rule; they provided only a laundry list of factors considered by the investment banker, which the Defendants had employed to render an opinion as to the fairness of the transaction. In *Howing I*, we concluded that the Rule requires a "reasonably detailed analysis of the various financial valuation methods discussed by the Rule and the weights attached thereto." *Howing I*, 826 F.2d at 1479. Because the proxy statement failed to provide a reasonably detailed analysis applying the various valuation methods and the weights attached thereto, we found that the Defendants failed to comply with the disclosure obligations imposed by Rule 13e-3. *Id.*

We also reversed the district court's determination that, "since there is no evidence of any breach of fiduciary duty owed by the defendants, and the merger was neither unauthorized by statute, illegal nor ultra vires under Ohio corporation law, the Ohio statutory appraisal right constituted the plaintiffs' exclusive state law remedy." *Id.* at 1474. We remanded the case, instructing the district

court (1) to reconsider the Defendants' failure to provide the information required by the instructions to Item 8 of Schedule 13E-3; (2) to consider issues of materiality of the Defendants' omissions under Rule 13e-3; and (3) to decide the state-law breach-of-fiduciary-duty claims and, if necessary, make detailed findings of fact and conclusions of law concerning the claim asserted under the state standard of fiduciary duty. We denied the Defendants' petition for rehearing and suggestion for rehearing en banc. The Supreme Court denied the Defendants' petition for certiorari.

2. The District Court's Second Judgment in Favor of the Defendants

Upon remand, the district court again granted summary judgment in favor of the Defendants. Although the Defendants had, as we had determined, failed to discuss in reasonable detail the net book, going-concern, or liquidation value, or the weights attached thereto in arriving at their fairness opinion, the district court found that such a discussion would not have provided a shareholder with information that was material under the standard set forth in *TSC Industries v. Northway, Inc.*, 426 U.S. 438 (1976). *TSC* states that "[a]n omitted fact is material if there is a substantial likelihood that a reasonable shareholder would consider it important in deciding how to vote." *TSC*, 426 U.S. at 449. The district court also concluded that, because of the "extraordinary" procedural steps taken to safeguard the interests of the public shareholders, the Defendants violated no state-law fiduciary duty.

3. *Howing II*: The Second Appeal to the Sixth Circuit

After the district court's second judgment in favor of the Nationwide Defendants, the Plaintiffs again appealed to this court. *See Howing Co. v. Nationwide Corp.*, 927 F.2d 263 (6th Cir. 1991) (hereinafter "*Howing II*"). We first considered the district court's conclusion that the

omission of the disclosures required by Rule 13e-3 did not meet the *TSC* standard of materiality. Agreeing with the district court that the *TSC* standard of materiality applied to Rule 13e-3 transactions, we held that:

> the clear and specific language of the instructions to Item 8 creates in effect a presumption that a discussion of book, going concern and liquidation value in the proxy statement would be material to a reasonable shareholder. The presumed fact—that the investor would likely find disclosure of such information significant—follows from Item 8's insistence that the information be stated.

Howing II, 927 F.2d at 265. We then held that the Defendants had not rebutted this presumption, and therefore, we reversed the district court's grant of summary judgment in their favor.

Additionally, we considered the Plaintiffs' state-law breach-of-fiduciary-duty claims. We first held that the only arguable Ohio-law claim is against Nationwide Mutual in its capacity as majority shareholder of Nationwide Corporation.[2] We next noted that, under Ohio law, although a majority shareholder may have a right to "cash out" the minority shareholders for any reason, the majority shareholder has a fiduciary duty to pay a "fair" price and *fully disclose all relevant facts about the value of the corporation whose stock it is buying.* The Defendants' failure to disclose all relevant information regarding valuation, we held, supports a state-law breach-of-fiduciary-duty claim against Nationwide Mutual. We, therefore, also reversed the district court's grant of summary judgment for the Defendants on the state-law breach-of-fiduciary-duty claim. We remanded the case to the district court for trial of both claims.

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[2] The Plaintiffs did not sue the directors of Nationwide Corporation. *See Howing II*, 927 F.2d at 267.

4. The Supreme Court's Remand to the Sixth Circuit

After *Howing II*, the Defendants sought review in the Supreme Court. The Court granted certiorari, vacated our judgment, and remanded the case for reconsideration in light of an intervening precedent, *Virginia Bankshares, Inc. v. Sandberg*, 501 U.S. ——, 111 S. Ct. 2749, 115 L.Ed.2d 929 (1991).

II.

Virginia Bankshares, a five to four decision, presented two issues to the Supreme Court. The first was the materiality of the claimed deficiencies in the proxy statement. The Court's resolution of that issue in no way undercuts our prior materiality determination in this case. The second issue was causation of damages to minority stockholders by the defective proxy statement. Justice Souter's majority opinion first discussed the Court's previous consideration of the causation issue in the context of the implied private right of action arising under § 14(a) of the Securities Exchange Act of 1934. It summarized *Mills v. Electric Auto-Lite*, 396 U.S. 375 (1970), which involved a merger where the majority shareholder controlled half the stock, but needed the votes of two-thirds to gain approval. After issuing a materially misleading proxy solicitation, the majority shareholder obtained approval by the necessary two-thirds. Proof that individual affirmative votes sufficient to alter the outcome were cast in reliance upon the misstatement and would have been cast against it given full and fair disclosure, the *Mills* court noted, would have presented an evidentiary morass of epic proportions.

The *Mills* Court avoided this evidentiary morass. It held that one could establish causation of damages by a materially misleading proxy solicitation by showing that minority votes necessary and sufficient to authorize the transaction had been given in accordance with the tenor of the solicitation. The Court concluded that, given a finding of materiality, a shareholder need only prove that

the proxy solicitation was an essential link in the accomplishment of the transaction. *Mills*, 396 U.S. at 385.

A. The *Schlick* Theory

Unlike the Court in *Mills*, the *Virginia Bankshares* Court had before it the claims of minority shareholders whose votes were not necessary for the authorization of the transaction. In the *Virginia Bankshares* decision, the majority rejected the first of the minority shareholders' two theories of causation.[3] The first theory, similar to one adopted by the Second Circuit in *Schlick v. Penn-Dixie Cement Corp.*, 507 F.2d 374 (2d Cir. 1974), was that the director' desire to avoid minority shareholders' ill will by use of a misleading proxy solicitation should provide the causal nexus between the proxy statement and the merger. (Hereinafter, "the *Schlick* theory"). The theory draws support from the premise that, in the face of an unfavorable minority shareholder vote, a board of directors might well choose not to go forward with a transaction—even though the majority shareholder had the raw voting power to authorize the transaction. The Court rejected this theory because it would give rise to speculative claims and procedural intractability. "Causation would turn on inferences about what the corporate directors would have thought and done without the minority shareholder approval unneeded to authorize action." *Virginia Bankshares*, 501 U.S. at ——, 111 S. Ct. at 2764-65, 115 L. Ed.2d at 953-54.

B. The Loss-of-State-Law-Remedy Theory

The minority shareholders in *Virginia Bankshares* derived their second theory of causation from Virginia's law of postmerger ratification. They noted that minority approval, though unneeded to authorize the transaction,

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[3] The four dissenters would have approved this theory of causation. *See Virginia Bankshares*, 501 U.S. at ——, 111 S. Ct. at 2770-73, 115 L. Ed.2d at 960-63.

would preclude a minority suit attacking the merger based on the alleged conflict of interest on the part of a director of the merged corporation. They argued that causation should be recognized when a misleading proxy statement induces minority shareholders to forfeit such a state-law remedy.

The Court in *Virginia Bankshares*, although not rejecting this theory, declined to decide its merits. The Court found that "there is no indication in the law or facts before us that the proxy solicitation resulted in any such loss [of the state law remedy]," *Virginia Bankshares*, 501 U.S. at ——, 111 S. Ct. at 2765-66, 115 L. Ed.2d at 954-55, because a favorable minority vote *induced by a materially misleading proxy solicitation* would not, under Virginia law, render the transaction invulnerable to such later attack by the minority.[4]

III.

The Supreme Court's remand for reconsideration in light of *Virginia Bankshares* raises two issues relevant to causation. The first is whether the *Virginia Bankshares* analytical framework applies to this claim, which, unlike *Virginia Bankshares*, arises under § 13(e), not § 14(a). The second is whether, assuming the *Virginia Bankshares* analytical framework applies, the Plaintiffs have asserted and supported an acceptable theory of causation.

A. The Applicability of the *Virginia Bankshares* Analytical Framework

Defendants acknowledge that *Virginia Bankshares* arose under § 14(a), while this case arises under § 13(e). They contend, however, that the *Virginia Bankshares* analysis of causation applies. They support this conten-

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[4] Justice Kennedy's dissenting opinion, which Justices Marshall, Blackmun, and Stevens joined, also would have accepted the loss-of-state-law-remedy theory of causation. *See Virginia Bankshares*, 501 U.S. at ——, 111 S. Ct. at 2773, 115 L. Ed.2d at 963-64.

tion by citing *Howing I*, in which, relying on the fact that § 13(e) was patterned after § 14(a) and parallels its language, this court concluded that, just as one exists under § 14(a), an implied private right of action exists under § 13(e). The Defendants argue, therefore, that the Supreme Court's § 14(a) causation analysis applies to private actions arising under § 13(e).

The Plaintiffs contend that the *Virginia Bankshares* analytical framework does not apply to § 13(e) claims. They contend that, because Rule 13e-3 imposes special disclosure obligations that are absent under Rule 14a-9, the dangers of speculative, hazy factual issues that concerned the Supreme Court in *Virginia Bankshares* do not arise under § 13(e). They further contend that the raw power of the majority shareholder to approve the transaction—the very power whose abuse created the need for § 13(e) and its unique disclosure requirements—renders the *Virginia Bankshares* analysis of causation inappropriate. If *Virginia Bankshares* means that the causation requirement can never be established when the minority shareholders lack sufficient votes to block the transaction, they argue, then the private right of action under § 13(e) would provide only an illusory sort of protection—protection that is unavailable in the archetype of the situations that § 13(e) governs.

If we interpreted *Virginia Bankshares* as holding that minority shareholders who lack sufficient votes to block a transaction can never establish causation of damages, then we would agree with the Plaintiffs. It would make little sense to hold that the protection of an implied private right of action exists under § 13(e), but that causation can never be established in the case where minority shareholders, who lack sufficient votes to block the transaction, have their greatest need for such protection. We do not, as is explained *infra*, interpret *Virginia Bankshares* so broadly.

Several authorities do appear to have assigned to the *Virginia Bankshares* holding, with respect to causation of

damages, such a broad interpretation.[5] This overestimation of the scope of the holding in *Virginia Bankshares* is understandable. Justice Souter's majority opinion at one point frames the issue before the Court in broad terms: "The second issue before us . . . is whether causation of damages compensable through the implied private right of action under § 14(a) can be demonstrated by a member of a class of minority shareholders whose votes are not required by law or corporate bylaw to authorize the transaction giving rise to the claim." *Virginia Bankshares*, 501 U.S. at ——, 111 S. Ct. at 2761, 115 L. Ed.2d at 949.

The Court, however, did not actually decide the broad question that it framed. It rejected only the narrow *Schlick* theory. The Court's express refusal to address the merits of the loss-of-state-law-remedy theory is inconsistent with the broader interpretation of the opinion. If minority shareholders who lack sufficient votes to block a transaction could never establish causation, as the Nationwide Defendants contend, it would have made no sense for the Court expressly to refuse to address the merits of the loss-of-state-law-remedy theory. That

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[5] *See Roosevelt v. E.I. Du Pont De Nemours & Co.*, 1992 [CCH] Fed. Sec. L. Rep. ¶ 96,527 (D.C. Cir. March 4, 1992) ("[T]he Court refused to extend the *Borak* section 14(a)/Rule 14a-9 right of action to minority shareholders who lacked the votes needed to block the merger that gave rise to the claim. . . . Because the complaining shareholders in *Virginia Bankshares* lacked the power to block the merger, the Court allowed no private right of action."); *Scattergood v. Perelman*, 945 F.2d 618, 624-25 (3d Cir. 1991) ("[W]hen a majority shareholder of a company pursues a freeze-out merger, the chain of causation between a pre-merger misrepresentation and the price received under the merger is broken . . . ."); L. Loss, *Fundamentals of Securities Regulation*, 948 (1991 Supp.) ("The analogous question—whether causation of damages could be shown by a member of a minority class of shareholders whose votes were not required by law or corporate bylaw to authorize the corporate action subject to the proxy solicitation—received a negative answer in *Virginia Bankshares v. Sandberg*, 111 S. Ct. 2749 (1991).").

theory, and indeed, any other the *Virginia Bankshares* plaintiffs could offer, would be without merit.

Thus, we interpret *Virginia Bankshares* more narrowly than do the Defendants. Our narrower interpretation, however, undercuts the Plaintiffs' argument that the *Virginia Bankshares* § 14(a) analytical framework should not apply at all to claims under § 13(e). Given our rejection of the Defendants' contention that *Virginia Bankshares* requires rejection of *all* nonvoting theories of causation, the Plaintiffs' complaint that the § 13(e) private action provides only an illusory sort of protection collapses. Because we conclude that nonvoting theories of causation can support a § 13(e) claim, minority shareholders with insufficient votes to block a transaction have protection.

While we cannot derive a general standard of causation from *Virginia Bankshares*, we can apply the Court's analysis. The Court stated that:

> where a legal structure of private statutory rights has developed without clear indications of congressional intent, the contours of that structure need not be frozen absolutely . . . . Faced . . . with . . . a claim for equality in rounding out the scope of an implied private statutory right of action, we look[] to policy reasons for deciding where the outer limits of the right should lie.

Virginia Bankshares, 501 U.S. at ——, 111 S. Ct. at 2764, 115 L. Ed. 2d at 953. The Court then subjected the plaintiffs' *Schlick* theory of causation to such a policy analysis and rejected it, concluding that the likelihood of speculative claims and procedural intractability made the adoption of that theory unwise.

B. Application of *Virginia Bankshares*' Analytical Framework to the Plaintiffs' Theory of Causation

Proceeding from the proposition that the *Virginia Bankshares* analysis of causation applies to this action

under § 13(e), and noting the factual similarities of the two cases, the Nationwide Defendants contend that the Plaintiffs cannot demonstrate causation. They contend that, under *Virginia Bankshares*, minority shareholders can never establish causation when a majority shareholder holds sufficient raw voting power to authorize the transaction. The Plaintiffs, in response, distinguish their case from *Virginia Bankshares*. They correctly note that the state-law remedy of appraisal was unavailable to the plaintiffs in *Virginia Bankshares*. *See Virginia Bankshares*, 501 U.S. at —— n.14, 111 S. Ct. at 2766 n.14, 115 L. Ed.2d at 955 n.14. Such a remedy was, however, available to the minority shareholders of Nationwide Corporation, who are the class Plaintiffs here. *See* Ohio Rev. Code § 1701.85.

1. Recognition of the Loss-of-State-Law-Remedy Theory

We must first determine whether the Plaintiffs loss-of-state-law-remedy theory of causation can support a § 13(e) claim. In *Virginia Bankshares*, four members of the Court concluded that this theory could support a § 14(a) claim. *See Virginia Bankshares*, 501 U.S. at ——, 111 S. Ct. at 2773, 115 L. Ed.2d at 963-64 (Kennedy, J., dissenting). The five majority justices refused to consider the theory because they found that the case did not present it.

This case clearly presents the question left unresolved by the majority in *Virginia Bankshares*. We are not, however, completely without guidance in the resolution of this question. In *Virginia Bankshares*, the Court indicated, as we noted *supra*, that we should look to policy reasons to assess the legitimacy of a theory of causation. *See Virginia Bankshares*, 501 U.S. at ——, 111 S. Ct. at 2764, 115 L. Ed.2d at 953. We must, therefore, look first to *Mills v. Electric Auto-Lite*, 396 U.S. 375 (1970), to determine what policy considerations motivated the Court to accept the theory of causation presented in that case. We also must look to *Virginia Bankshares* to deter-

mine what policy considerations motivated the Court to reject the *Schlick* theory of causation.

In *Mills*, in which some minority votes were needed, the Court indicated that its decision was motivated by its desire to avoid the impracticalities of determining which votes were affected by the misleading proxy solicitation and to resolve doubts in favor of those that the statute was designed to protect. The decision supports, it points out, the fair corporate suffrage that Congress sought, by § 14(a), to require. The policies recognized and relied upon by *Mills* support the Plaintiffs' causation theory.

But the Plaintiffs' causation theory differs from that accepted in *Mills*. In *Mills*, the Court effectively created a conclusive presumption that a materially misleading proxy solicitation affects the outcome of a shareholder vote on the transaction if some minority votes are needed. Such a presumption obviously defies logic when the minority shareholders lack sufficient votes to affect the outcome. In this case, because Nationwide Mutual controlled 85% of the votes, the misleading proxy solicitation could not have affected the result of the vote. The Plaintiffs, however, contend that a different inference should be made—that the misleading proxy statement was an "essential link" in thier decisions not to pursue their appraisal remedies.

Virginia Bankshares provides some guidance. The Plaintiffs submit that their loss-of-state-law-remedy theory avoids the dangers of speculation, which caused the *Virginia Bankshares* Court to reject the *Schlick* theory of causation. Clearly, there is an element of speculation involved in the Plaintiffs' theory. It requires an inference that, given full and fair disclosure, members of the Plaintiff class would have (1) voted against the transaction or not voted, thus qualifying for the appraisal remedy; and (2) exercised their appraisal rights within the statutorily prescribed ten-day time limitation. *See* Ohio Rev. Code § 1701.85. This element of speculation, how-

ever, appears to us no greater than that involved in *Mills*, where the Court adopted a presumption that, given full and fair disclosure, members of the plaintiff class would have voted against the proposed transaction.

In *Virginia Bankshares*, with reference to the *Schlick* theory of causation that the Court rejected, the Court said:

> Causation would turn on inferences about what the corporate directors would have though and done without the minority shareholder approval unneeded to authorize action. A subsequently dissatisfied minority shareholder would have virtual license to allege that managerial timidity would have doomed corporate action but for the ostensible approval induced by a misleading statement, and opposing claims of hypothetical diffidence and hypothetical boldness on the part of directors would probably provides enough depositions in the usual case to preclude any judicial resolution short of the credibility judgments that can come only after trial.

Virginia Bankshares, 501 U.S. at ——, 111 S. Ct. at 2765, 115 L. Ed.2d at 953. The difference between the presumption required by the *Schlick* theory that the Court rejected in *Virginia Bankshares* and the presumption required by the *Mills* theory that Court accepted lies in the power to act. In *Mills*, the Court deemed a presumption, with respect to minority shareholder action within the scope of their enforceable rights, likely enough. In *Virginia Bankshares*, however, the Court deemed a presumption, with respect to the possible actions of the involved directors, too speculative. *Virginia Bankshares*, 501 U.S. at ——, 111 S. Ct. at 2765, 115 L. Ed.2d at 950. Unlike this rejected *Schlick* theory, the Plaintiffs' loss-of-state-law-remedy theory derives its causal link from the enforceable terms—including the right to appraisal—of the parties' corporate relationship, not from anything so amorphous and speculative as the directors' apprehension of the ill will of the minority shareholders.

The Plaintiffs' loss-of-state-law-remedy theory relies on a presumption that is no more speculative than the presumption made by the Court in *Mills*, and less so than the one rejected by the Court in *Virginia Bankshares*. The presumption concerns likely action by shareholders, and the causal link arises from the enforceable terms of the corporate relationship.

Finally, there is another reason we favor recognition of the Plaintiffs' theory of causation. We previously have indicated our belief that Congress intended that an implied private right of action arise under § 13(e). Having found such congressional intent, we would certainly be hesitant to conclude that Congress also intended that causation could not be demonstrated in any case where the minority shareholders lack sufficient votes to block the transaction. As the Plaintiffs note, this situation arises in the archetypal going-private transaction. Such shareholders are least able to protect their own interests, and they have the greatest need for the protection provided by the private right of action. These shareholders lack even the protection of sufficient numbers to vote down the proposed transaction. We will not deprive them of the protection of § 13(e).

In summary, we draw support for our recognition of the Plaintiffs' theory of causation from several sources. First, three current members of the Supreme Court have indicated their support for the theory, while the remainder of the Court has not determined its merits. Second, if, as the Nationwide Defendants contend, minority shareholders without sufficient voting power to prevent a transaction were categorically unable to demonstrate causation, we believe the Court would have resolved *Virginia Bankshares* on that broader ground. Third, the element of speculation required by the Plaintiffs' theory is no greater than that required by the theory accepted by the Court in *Mills*. Finally, we would be hesitant to hold that Congress intended to provide the protection of an implied right of action, but that causation could never be established in

those cases where the minority shareholders, lacking sufficient votes to block the transaction, had their greatest need for such protection.

2. Application of the Loss-of-State Law-Remedy Theory to the Facts of This Case

Given our conclusion that the loss of a state-law remedy provides an acceptable theory of causation supportive of a § 13(e) action, we must next decide if, in fact, the Plaintiffs have supported their theory of causation. Under Ohio law, the minority stockholders could have sought appraisal if they had voted against the transaction or had not voted, and then selected appraisal within the statutorily prescribed ten-day time limitation. *See* Ohio Rev. Code § 1701.85. The Nationwide Defendants, however, argue that the record actually refutes these Plaintiffs' claims of causation.

The Defendants base their argument upon the contents of the proxy solicitation and the statements attributed to two of the class Plaintiffs. They claim that, far from misleading the minority shareholders, the proxy solicitation disclosed the pendency of the *Efros* litigation, which was later consolidated with this case. They further note that the proxy solicitation contained a "Summary of Steps in Dissenting Shareholder Procedure," which explained how to obtain appraisal. Finally, they note that a named Plaintiff, McLellan, admitted he was "aware that under Ohio law with respect to the merger that [he] had appraisal rights as a stockholder of Nationwide Corporation" and that he "decided not to pursue those appraisal rights even though [he] believed that the $42.50 merger price was inadequate." Additionally, the Defendants note that Mr. Hirsch, managing partner of the Howing Company, admitted that he was aware of Howing's appraisal rights, but elected not to pursue them because he was told that "there was already a litigation started as a class action suit," and he concluded that "there was no point in going after" appraisal rights. Thus, the Nationwide

Defendants argue, the named Plaintiffs were not misled by the material omissions; they thought the merger price inadequate, but consciously chose to forego their appraisal remedy.

We cannot accept the Defendants' argument. In *Mills*, the Court discussed a requirement of proof of whether a defect in the proxy solicitation actually had a decisive effect on the voting. The Court held:

> Where there has been a finding of materiality, a shareholder has made a sufficient showing of causal relationship between the violation and the injury for which he seeks redress if, as here, he proves that the proxy solicitation itself, rather than the particular defect in the solicitation materials, was an essential link in the accomplishment of the transaction.

Mills, 396 U.S. at 385. Similarly, to paraphrase the Court, where there has been a finding of materiality, a shareholder has made a sufficient showing of causal relationship between a violation of § 13(e) and the loss of his state-law remedy if, as here, he proves that the proxy solicitation was an essential link in the chain of events that deprived him of his state-law remedy.

Application of the *Mills* presumption in this case provides a strong incentive for issuers to comply with § 13(e) and accords with probable shareholder responses had there been full and fair disclosure. The Plaintiffs' decisions with respect to appraisal might well have been different had they received the full and fair disclosure to which they were entitled. Although McLellan, and Hirsch of the Howing Company, admit that a strategic decision led them to forego their appraisal remedies and instead pursue this litigation, the Plaintiffs note that, had the Nationwide Defendants provided the information required by Rule 13e-3, an appraisal remedy would have been more attractive. Without the information required by Rule 13e-3, the appraisal remedy is less meaningful.

As Justice Kennedy indicated in his dissent in *Virginia Bankshares*, "minority shareholders will be in a better position to protect their interests with full disclosure." *Virginia Bankshares*, 501 U.S. at ——, 111 S. Ct. at 2772, 115 L. Ed.2d at 963 (quoting L. Loss, *Fundamentals of Securities Regulation* 1119-20 (1983)). These interests include the shareholders' interest in arriving at a fair price through an appraisal action.

Rule 13e-3 and § 13(e) embrace Congress' philosophy of full and fair disclosure of all material information in freeze-out transactions. Absent such disclosure, the value of a state-law appraisal remedy declines precipitously. The goal of § 13(e) and Rule 13e-3 is to provide shareholders with all of the information they need to make informed decisions with respect to their investments. Faced with a vote on a proposed merger, and a ten-day window in which they had to exercise or forsake the appraisal remedy, the minority shareholder-Plaintiffs had their greatest need for such disclosure. The Nationwide Defendants' failure to provide such disclosure forced the Plaintiffs to make these pressing, important decisions in an atmosphere of ignorance and confusion.

We hold that, based upon the loss of their appraisal remedy, the Plaintiffs have established causation supportive of their § 13(e) claim.

IV.

The Defendants make three additional arguments in suport of their contention that we should affirm the judgment of the district court. They first argue that *Virginia Bankshares* is inconsistent with the existence of a private right of action under § 13(e). Second, the Defendants argue that *Virginia Bankshares* is inconsistent with our conclusion that the omissions in the proxy solicitation in this case were material facts. Third, they even argue that *Virginia Bankshares* demonstrates the error of our reasoning with respect to the existence of a

state-law breach-of-fiduciary-duty claim.[6] After giving thorough consideration to each of these arguments, we find them without merit. We conclude that *Virginia Bankshares* in no way undermines our *Howing I* analysis of the private right of action issue or our *Howing II* analysis of the materiality and state-law breach-of-fiduciary-duty issues.

V.

The Supreme Court remanded this case for reconsideration in light of *Virginia Bankshares*. From the foregoing analysis, we conclude that the Plaintiffs' loss of their state-law appraisal remedy establishes causation consistent with *Virginia Bankshares*. We also reject the Defendants' other arguments, as indicated *supra*.

For the foregoing reasons, we REVERSE the judgment of the district court and REMAND the case for trial.

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[6] The dissent indicates its discomfort with our continued approval of the claim for breach of fiduciary duty. For the reasons articulated in *Howing II*, we reaffirm our decision that the district court should not have granted summary judgment for the Defendants with respect to this issue. *See Howing II*, 927 F.2d at 267-70.

RALPH B. GUY, JR., Circuit Judge, dissenting. Although I substantially agree with Judge Brown's thorough analysis of the *Virginia Bankshares* decision, I must dissent from that portion of the majority opinion which applies that analysis to the facts of this case. I also write separately to express my doubt that Ohio law would recognize the plaintiff-shareholders' fiduciary duty claim, when it seeks only additional compensation for their shares.

I.

Like the majority, I read *Virginia Bankshares* as advancing the possibility that minority shareholders lacking sufficient votes to block a corporate transaction may establish causation for purposes of a section 14(a) suit by showing that the false or misleading proxy statement resulted in the loss of a state remedy. Assuming that there is indeed an analogous private right of action under section 13(e),[1] I agree that the "lost state remedy" causation theory may be instructive in this case which, like *Virginia Bankshares*, involves minority shareholders' complaints regarding full disclosure in the contested proxy statements. I do not agree, however, that the facts of this case demonstrate an induced forfeiture of the appraisal remedy, and I would therefore decline to allow *Howing* to stand for our circuit's full-fledged endorsement of the "lost remedy" theory.

The majority's adoption of the lost-remedy argument is based on an inference that disclosure of the desired information would have moved the plaintiffs to vote against the transaction (or abstain from voting) and to exercise their appraisal rights within the statutorily prescribed ten-day period. As prior decisions in this case have made clear, however, none of the named plaintiffs voted in

[1] I say "assuming" because, although I joined that part of this court's original opinion in this case which found a private right of action, I have since had second thoughts and now have serious doubts about that conclusion.

favor of the merger. In other words, there can be no suggestion that these plaintiffs were duped by the allegedly misleading proxy statement into voting for the merger on the mistaken belief that the transaction would be in their best interests. In general, a shareholder's failure to vote upon receipt of a defective proxy statement—and a subsequent failure to assert the appraisal rights on time—may just as readily suggest that the dissenting shareholder, aware of the proxy's defects and believing the shares to be worth far more, intends to challenge those defects and seek damages in a separate action.

That this alternative inference is equally as plausible is demonstrated by the facts of this case. Even before the proxy materials were disseminated, a minority shareholder, Belle Efros, sought to enjoin the merger for, among other things, paying the public shareholders "a grossly inadequate price." Complaint at 6, *Efros v. Nationwide Corporation*, No. C-2-82-1385 (S.D. Ohio). This early Efros litigation, with which the present case was eventually consolidated, was then addressed in the proxy materials, which also explained how dissatisfied shareholders may assert their appraisal rights.

Even more significantly, the named plaintiffs' own admissions refute the inference that the proxy statement induced them to forfeit the appraisal remedy. Plaintiff McClellan conceded that he "elected not to pursue" his appraisal rights even though he believed that the $42.50 merger price was inadequate. Similarly, the managing partner of the Howing Company stated that shortly after he received the proxy, he, in consultation with his broker, decided not to vindicate his dissatisfaction with the price through appraisal but to rely instead on the outcome of the Efros litigation. Further, in arguing the motion for class certification, plaintiffs' counsel stated that they had chosen the more economical route of the class action over individual appraisal actions. The district court's order conditionally certifying the case as a class action essen-

tially confirmed that the appraisal remedy had been considered and deliberately abandoned:

> Although plaintiffs admit that they could have invoked the protections of Ohio's dissenting shareholder's statute . . . they have chosen to pursue their claims under the federal securities laws and the common law of Ohio.

Given these undisputed facts, I would decline to find that the plaintiffs here were duped or misled into forfeiting the right to assert their objection to the merger price in an appraisal action. Thus, this seems to me a poor case for deciding whether this circuit should adopt the "lost state remedy" theory alluded to in *Virginia Bankshares.*

II.

In addition, I note briefly my discomfort with the majority's continued approval of the claim for breach of fiduciary duty. I understand the Ohio Supreme Court cases of *Armstrong v. Marathon Oil Co.*, 513 N.E.2d 776 (1987), and *Stepak v. Schey*, 553 N.E.2d 1072 (1990), to mean that while an action for a breach of fiduciary duty may indeed be maintained outside an appraisal proceeding, such action will not be countenanced if it seeks only "to overturn or modify the fair cash value determined in a cash-out merger." *Schey*, 553 N.E.2d at 1074. These two cases, according to a recent Ohio Court of Appeals decision,

> made it clear that a shareholder cannot disguise what is essentially a cause of action for an appraisal of the value of stock by bringing that cause of action under an allegation of breach of fiduciary duty and fraud. The hallmark for determining whether a cause of action is in essence a disguised request for an appraisal of the value of the stock is the damages which are sought for the cause of action.

Gergely v. Van Voorhis, No. E-90-36, 1992 Ohio App. LEXIS 384 (1992) at *11 (Ohio App. Jan. 31, 1992) (citations omitted). *See also* David L. Kinsella, *Ohio's Newest Claim Outside of an Appraisal for Dissenting Shareholders in a Merger Situation—Breach of Fiduciary Duty*, 16 U. Dayton L. Rev. 773 (1990). It seems clear that what these plaintiffs seek is more money for their shares rather than, for example, the disgorgement of profits or the rescission of the merger.

I would affirm the district court's decision.

UNITED STATES COURT OF APPEALS
FOR THE SIXTH CIRCUIT

Case No. 89-4084

HOWING COMPANY; DOUGLAS MCCLELLAN,
Plaintiffs-Appellants,

v.

NATIONWIDE CORPORATION;
NATIONWIDE MUTUAL INSURANCE COMPANY,
Defendants-Appellees

ORDER

[Filed November 25, 1992]

Upon consideration of appellee's motion to recall the mandate pending application to the Supreme Court for writ of certiorari,

It is ORDERED that the motion be and is hereby is GRANTED. The issuance of the mandate shall be stayed until February 4, 1993.

ENTERED BY ORDER OF THE
COURT

/s/ Leonard Green
LEONARD GREEN
Clerk

UNITED STATES COURT OF APPEALS
FOR THE SIXTH CIRCUIT

No. 89-4084

HOWING COMPANY; DOUGLAS MCCLELLAN,
Plaintiffs-Appellants,

v.

NATIONWIDE CORPORATION;
NATIONWIDE MUTUAL INSURANCE COMPANY,
Defendants-Appellees.

ORDER

[Filed November 4, 1992]

BEFORE: MERRITT, Chief Judge; GUY, Circuit Judges; and BROWN, Senior Circuit Judge.

The court having received a petition for rehearing en banc, and the petition having been circulated not only to the original panel members but also to all other active judges of this court, and no judge of this court having requested a vote on the suggestion for rehearing en banc, the petition for rehearing has been referred to the original hearing panel.

The panel has further reviewed the petition for rehearing and concludes that the issues raised in the petition were fully considered upon the original submission and decision of the case. Accordingly, the petition is denied.

ENTERED BY ORDER OF THE
COURT

/s/ Leonard Green
LEONARD GREEN
Clerk

UNITED STATES COURT OF APPEALS
FOR THE SIXTH CIRCUIT

Case No: 89-4084

HOWING COMPANY; DOUGLAS MCCLELLAN,
Plaintiffs-Appellants,

v.

NATIONWIDE CORPORATION;
NATIONWIDE MUTUAL INSURANCE COMPANY,
Defendants-Appellees

ORDER

[Filed April 13, 1992]

Upon consideration of appellee's motion for certification of question of state law to the Ohio Supreme Court,

It is ORDERED that the motion be and it hereby is DENIED.

ENTERED BY ORDER OF THE
COURT

/s/ Leonard Green
LEONARD GREEN
Clerk

UNITED STATES COURT OF APPEALS
FOR THE SIXTH CIRCUIT

No. 89-4084

HOWING COMPANY, DOUGLAS MCLELLAN,
Plaintiffs-Appellants,

v.

NATIONWIDE CORPORATION,
NATIONWIDE MUTUAL INSURANCE COMPANY,
Defendants-Appellees.

On Appeal from the United States District Court
for the Southern District of Ohio

Decided and Filed March 6, 1991

Before: MERRITT, Chief Judge; GUY, Circuit Judge; BROWN, Senior Circuit Judge.

MERRITT, Chief Judge, delivered the opinion of the court, in which BROWN, Senior Circuit Judge, joined. GUY, Circuit Judge (p. 13) delivered a separate dissenting opinion.

MERRITT, Chief Judge. In this securities action by minority public shareholders arising from a freeze-out

merger of a subsidiary, Nationwide Corporation, with its parent, Nationwide Mutual, which at the time of the merger owned approximately 85% of the shares of the subsidiary, we previously reversed the District Court's dismissal of plaintiffs' claims under SEC Rule 13e-3, governing going-private transactions or freeze-out mergers; and we then remanded the case to the District Court for further proceedings. We refer the reader to our earlier opinion for a detailed statement of the facts and the law applicable to such mergers under Rule 13e-3. *See Howing Co. v. Nationwide Corp.*, 826 F.2d 1470 (6th Cir. 1987), *cert. denied*, 108 S. Ct. 1008 (1988).

I. Materiality Under Rule 13e-3

In our earlier opinion, we found that the defendant corporations in their going-private offer to the minority public shareholders had violated Item 8 required under Rule 13e-3 by making no effort to state, discuss or explain in reasonable detail the net book value, the going concern value or the liquidation value of the company whose minority interests were purchased. On remand, the District Court concluded that such a discussion would not have provided a shareholder with information of "material" value under the legal standard of "materiality" in securities transactions set out in *TSC Indus. v. Northway, Inc.*, 426 U.S. 438 (1976). The District Court therefore granted summary judgment for the defendant corporations which were responsible for the proxy statement we had previously found defective under Item 8 of Rule 13e-3.

The District Court based its grant of summary judgment on the ground that it is so clear and beyond dispute that the information on these values would not be of significance to a shareholder that no reasonable trier of fact—in this case a jury—could reach a contrary conclusion. We do not agree that the insignificance of the information is so clear, and we therefore remand the case for trial. The instructions for Item 8 of Rule 13e-3, as we

have previously observed, are clear and specific in their requirement for a discussion of book, going concern and liquidation value in the fairness section of the proxy statement. They say that the issuer "should discuss in reasonable detail," among other things, the net book value, going concern value and liquidation value and "to the extent practicable, the weight assigned each factor." This and other information is specifically required by the SEC because these freeze-out transactions, unlike tender offers and other market transactions, are conducted outside the discipline of the competitive market place in which freedom of contract is the norm. As the SEC has noted, such "going private transactions present an opportunity for overreaching" and are "coercive" because of "the lack of arms-length bargaining and the inability of [minority shareholders] to influence corporate decisions to enter into such transactions." [1] Exchange Act Release No. 34-17719, *reprinted in* 3 Fed. Sec. L. Rep. (CCH) ¶ 23,709, at 17, 245-42 (April 13, 1981).

Although we agree with the District Court that the general *TSC* standard of materiality is applicable to transactions governed by Rule 13e-3, the clear and specific language of the instructions to Item 8 creates in effect a presumption that a discussion of book, going concern and liquidation value in the proxy statement would

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[1] Most commentators, even those who disagree over the method and degree of regulation of going private transactions, agree with the SEC that, in certain contexts, going-private transactions present opportunity for abuse, similar to insider trading. *Compare* Brudney, *A Note on Materiality and Soft Information Under the Federal Securities Laws*, 75 U. Va. L.R. 723, 739 (1989) ("When a controlling block or a substantial portion of the corporation's stock is own by one person or a coherent group, corporate dealing in its own securities, particularly repurchase of its own securities, is not significantly different from insider trading"), *with* Easterbrook & Fischel, *Corporate Control Transactions*, 91 Yale L.J. 698, 707 (1982) ("Some going-private transactions may be motivated by a desire to exploit inside information rather than to reduce agency costs").

be material to a reasonable shareholder. The presumed fact—that the investor would likely find disclosure of such information significant—follows from Item 8's insistence that the information be stated.

The failure to state the information triggers the presumption which the defendants may then rebut in the normal way under Rule 301 of the Federal Rules of Evidence. If the party adverse to the presumption offers no evidence contradicting the presumption of materiality, the court will instruct the jury that it may presume the omissions are material. If the adverse party presents evidence suggesting the insignificance of the omitted information, the right of the plaintiffs to have the jury consider the significance of the information persists, and the jury may infer that the information would be significant, unless and until evidence has been received which would require a directed verdict for the defendants on the significance of the information. The persuasiveness of the evidence so far presented by the defendants does not rise to that level, and hence the District Court should not have granted summary judgment.

The Supreme Court has made use of rebuttable presumptions in analogous factual circumstances in securities law cases. In a 10b-5 action, the Court upheld the use of a rebuttable presumption of reliance where a company misled sellers of its stock by not disclosing that it was engaged in merger negotiations. *Basic Inc. v. Levinson*, 108 S. Ct. 978 (1988). The Court justified adopting this rebuttable presumption because of the "unnecessarily unrealistic evidentiary burden" that plaintiffs otherwise would have had in showing how they would have acted if the omitted information had been stated. *Id.* at 990. *See also Affiliated Ute Citizens of Utah v. United States*, 406 U.S. 128, 153-54 (1972) (upholding rebuttable presumption of reliance where material omission made in proxy statement). Similarly, in the instant case, in which the question is what "would be" the reaction of reasonable

shareholders to the information, the omission should raise a rebuttable presumption. The likelihood that the factors the SEC has enumerated in Item 8(b) will be material is sufficiently strong that omission of such factors without explanation of the reason for the omission will result in a rebuttable presumption of their materiality.

Establishing a presumption of materiality as to factors listed in Item 8(b) is in accord with other courts that have recognized the appropriateness of a "heightened" *TSC* materiality standard in coercive securities transactions such as this one. For example, in *Pavlidis v. New England Patriots Football Club, Inc.*, 737 F.2d 1227, 1231 (1st Cir. 1984), the First Circuit concluded that a heightened *TSC* standard should govern in a freeze-out merger where an allegedly misleading proxy statement was drafted at the direction of a shareholder who owned the controlling interest in a corporation at the time of a merger. Discussing materiality in the context of § 14(a) of the Securities Act and Rule 14a-9 promulgated thereunder, the Court found that certain facts may be material in the context of a "one-sided transaction" which otherwise would not be material in the context of an adversarial transaction. *Id.* Specifically, the First Circuit stated that, even though § 14(a) requires any party soliciting proxies to disclose all material information regardless of status or interest, a self-dealing insider may have a "heavier burden of disclosure" in meeting the § 14(a) disclosure requirements. *Id.; accord Plaza Securities Co. v. Fruehauf Corp.*, 643 F. Supp. 1535, 1544 (E.D. Mich. 1986) ("disclosures and nondisclosures [pursuant to Rule 13e-3] must be especially rigorous" where management involved in leveraged buyout designed to take company private); *Blanchette v. Providence & Worcester Co.*, 428 F. Supp. 347, 354 (D. Del. 1977) ("importance of a complete disclosure . . . is enhanced" where management controls the offeror corporation, as well as the offeree corporation; specifically, "management has a heavy burden to insure that disclosure is complete and nonmislead-

ing, especially with respect to shareholders whose interests may differ from their own").

In this action, defendants have not rebutted this presumption so as to avoid trial because they have not established the lack of significance of the information with sufficient clarity. The facts do not justify the grant of summary judgment on the ground that a reasonable investor would not find an explanation of book, going concern and liquidation value of any significance.

For example, plaintiffs' expert stated, and defendants' evaluator, First Boston Corp., appears to agree, that a relevant factor in a book value analysis is the multiplier, which is a number multiplied by book value to yield total selling price. According to plaintiffs' expert testimony, which is not effectively contradicted by defendants, insurance companies typically sell in a range from one to four times book value, with unhealthy companies selling in the lower range and more profitable companies selling at higher ratios. The cash out price of $42.50 paid by defendants is only slightly greater than book value, with a resulting multiplier of 1.025. Thus, it may well be that a reasonable shareholder would have found a discussion of this low multiplier (and of the multiplier range typical in purchases of insurance companies) important in deciding how to vote his shares.

We note that determining the value of a company from its book value multiplied by some "appropriate" industry multiplier is often an inexact method of valuation because book value measures nothing more than the value of a company's assets (minus liabilities) at the time the assets are added to a company's books. Obviously, in some cases, book value multiplied by some industry multiplier will not be a useful method to calculate a company's value. Accordingly, the corporation would state in its proxy materials that book value is not relevant to the "fairness" opinion, setting forth the factors leading it to

this determination of irrelevancy. Where a defendant does base its "fairness" opinion in part on comparison of book value to the cash out price, it should discuss in reasonable detail the multiplier used and why that multiplier is appropriate. In the instant case, the record strongly suggests that defendants used book value as an important factor in determining the "fairness" of the transaction and that they sought to use a multiplier of one. Some discussion of book value and the appropriateness of this multiplier for a company like Nationwide Corp. was warranted in the proxy materials.

Likewise, defendants did not discuss in the proxy materials the going concern and liquidation values or explain why they were not discussed. Like book value, defendants merely stated in conclusory language that they had considered these factors without stating what they were, how they were derived or their significance. In the proceeding below, defendants claimed that liquidation and going concern values were considerably lower than the cash out price offered minority shareholders. They presented evidence that Nationwide Corp. had no significant assets which could be sold for more than their book value, that New York insurance law would have frozen more than half of the value of total shareholders' equity ($260 million out of $462.2 million) that could be distributed in a liquidation and that Nationwide Corp. lacked an independent sales force which would have greatly decreased its value if sold as a going concern.[2] *See Howing Co. v. Nationwide Corp.*, No. 1-83-1693, at 7-9 (S.D. Ohio, Nov. 16, 1989). In response, plaintiffs introduced

[2] The defendants contend that Nationwide Corp. sold its policies through captive agents who are associated with two affiliated companies. Since these agents made most of their income by selling the affiliated companies' policies, defendants claim that if Nationwide Corp. was liquidated or sold in pieces, these agents likely would have retained their associations with the affiliated companies rather than going with Nationwide Corp., which would have had the effect of reducing the going concern and liquidation values of the company.

plausible expert testimony which contradicted defendants' contentions and which suggested that liquidation and going concern values were higher than the cash out price offered to minority shareholders. Because reasonable minds could have differed on whether the omitted discussion of liquidation and going concern values would be significant to a reasonable shareholder, the District Court erred in not letting the jury make this determination.

II. State Law Fiduciary Claim

In our earlier opinion, we asked the District Court to consider plaintiffs' state law breach of fiduciary duty claims. On remand, the District Court concluded that no fiduciary duty could have been violated by Nationwide Corp. or Nationwide Mutual, the majority shareholder, because of the "extraordinary" procedural steps taken to safeguard the interests of the public shareholders of Nationwide Corp. The District Court therefore granted summary judgment for defendants.

Plaintiffs did not sue the directors of Nationwide Corp. for breach of fiduciary duty, only the corporate entity itself. Because such a fiduciary claim must be made against a corporation's directors, and may not be maintained against the corporation itself under a theory of vicarious liability, *see, e.g., Radol v. Thomas*, 772 F.2d 244, 258 (6th Cir. 1985), *cert. denied*, 477 U.S. 903 (1986), plaintiffs' only arguable claim is against Nationwide Mutual in its capacity as majority shareholder of Nationwide Corp.

On appeal, plaintiffs argue that Nationwide Mutual, as majority shareholder, had a strong fiduciary duty to pay a fair price and to make full disclosure, fiduciary duties they claim Nationwide Mutual breached.

Traditionally, shareholders did not owe any fiduciary obligations to each other; any shareholder voting its own shares presumably could act solely in its own self-interest. Recently, however, courts have come to recognize that a

majority shareholder can control the corporation for its own benefit, sometimes to the detriment of the minority shareholders, through the election of directors who favor its interests. Although courts acknowledge this potential conflict, the majority shareholder fiduciary duty that has developed is less stringent than the duty owed by a trustee under traditional notions of trust law. State courts, including the courts of Ohio whose law is applicable, have had difficulty establishing a workable standard defining the "fiduciary duties" of a majority shareholder that acquires the stock of public shareholders in a freeze-out merger. The normal principles of complete loyalty owed by a trustee to a beneficiary do not work because a majority shareholder in such situations has a built-in conflict of interest with the minority shareholders. Regular trustees, under normal principles of fiduciary duty, may not engage in self-dealing, purchase the assets of the trust or have personal interests in trust transactions that could affect their judgment. Restatement (Second) of Trusts § 170(1) comments a-c (1959). These same principles normally apply to other fiduciaries like guardians, lawyers, agents, officers and directors. Restatement of Restitution § 190 (1937). Going private transactions between majority and minority shareholders violate all these principles.

In deriving an appropriate fiduciary duty for majority shareholders, it may be helpful to think of fiduciary duties as enforcement devices for implementing the intent of the minority and majority shareholders as to what benefits and risks the parties would agree *ex ante* to share. *See* Hetherington, *Defining the Scope of Controlling Shareholders' Fiduciary Responsibilities*, 13 Canada-United States L.J. 103, 110 (1988). As commentators have noted, majority and minority shareholders would almost never agree to a traditional trust relationship because such a relationship would not be in either's economic interest. *See id.* at 126-27; *see also*, Easterbrook & Fischel, *Corporate Control Transactions*, 91 Yale

L.J. 698, 726 (1982). Buyers of stock in a corporation usually purchase the stock for the profits the company generates, whether paid out or retained, subject to the possibility that, lacking a controlling interest, the shareholder will be forced at any time to sell at a "fair price." So long as the minority shareholders are paid a "fair price" for their shares in the cash out merger, and statistics uniformly suggest that minority shareholders in such transactions are paid a substantial premium to the prevailing market price, there is no reason to expect *ex ante* that minority shareholders would want to limit the majority shareholder's ability to force minority shareholders to sell their shares, or, for that matter, to prevent the majority shareholder from receiving a premium for its shares. *See* Heatherington, *Defining the Scope of Controlling Shareholders' Fiduciary Responsibilities*, 13 Canada-United States L.J. 103, 126-127 (1988).

In accord with this rationale, the general rule that has developed regarding the majority shareholder's fiduciary duty is that a majority shareholder may "cash out" the minority shareholders for any reason, so long as the majority shareholder pays a "fair" price and fully discloses relevant facts about the value of the corporation whose stock it is buying. *See, e.g., Weinberger v. UOP, Inc.*, 457 A.2d 701 (Del. 1983). The Ohio Supreme Court seems to follow this general rule imposing a fiduciary duty on majority shareholders. *See, e.g., Armstrong v. Marathon Oil Co.*, 513 N.E.2d 776, 798 (Ohio 1987); *see also Crosby v. Beam*, 548 N.E.2d 217, 220 (Ohio 1989) (discussing somewhat analogous situation of controlling shareholder's duty in close corporation). On appeal, plaintiffs assert as one component of their breach of duty claim that, where a majority shareholder controls both sides of the transaction, the burden is on the majority shareholder to demonstrate the "entire fairness" of the transaction to minority shareholders. This argument follows the law of Delaware and other states. *See, e.g., Weinberger*, 457 A.2d 701.

Ohio law, while recognizing that a majority shareholder must pay minority shareholders a "fair price" for their shares, nonetheless limits recovery in almost every situation [3] to recovery under the state's appraisal statute, Ohio Rev. Code Ann. § 1701.85 (Supp. 1989). *See Armstrong*, 513 N.E.2d 776, 798; *see also Stepak v. Schey*, 553 N.E.2d 1072 (Ohio 1990). In *Armstrong*, minority shareholders asked the Ohio Supreme Court to adopt Delaware law and to inquire (as Delaware courts do) into the "entire fairness" of a cash out transaction. Such an inquiry would have allowed minority shareholders to present evidence (under the theory of breach of fiduciary duty) that the cash out price paid to them was unfair. 513 N.E.2d at 797-98. The Ohio Supreme Court rejected this argument, noting that a statutory proceeding is the sole means of determining the value of shares sold by minority shareholders in a cash out merger. *Id.* Because Ohio law as set forth in *Armstrong* dictates otherwise, plaintiffs' argument on appeal, that the district court applying Ohio law should have inquired into the "entire fairness" of the transaction, must fail.

Plaintiffs also contend that Nationwide Mutual did not disclose material facts concerning the merger price in its proxy statement. As to this issue, we find that summary judgment should not have been granted. Following the general statement of a majority shareholder's fiduciary duty, Ohio courts seem to acknowledge that a majority shareholder owes minority shareholders a fiduciary duty to disclose "pertinent facts concerning the merger." *Stepak*, 553 N.E.2d at 1078 (Holmes, J., concurring); *see also Armstrong*, 513 N.E.2d at 798 (acknowledging that other causes of action may be available under breach of

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[3] Extra-statutory damages are available where the merger or acts of the officers and directors are fraudulent, unlawful or *ultra vires*. *See Stepak v. Schey*, 553 N.E.2d 1072 (Ohio 1990) (Holmes, J., concurring). However, as we determined in our earlier opinion, there was no fraud or unlawful activity in this merger.

fiduciary duty claim so long as not seeking additional compensation under theory of inadequate price).

As we determined in Section I of this opinion, plaintiffs have presented evidence that defendants omitted material information in their proxy statement that is required by Rule 13e-3. On appeal, plaintiffs contend that the omission of this same information (required by Rule 13e-3), constitutes a violation of Nationwide Mutual's majority shareholder fiduciary duty. Because Ohio law seemingly permits limited recovery on the narrow ground that full disclosure was not made in the majority shareholder's proxy statement, the district court on remand should try this state law claim.

In effect, plaintiffs have only one claim (although stated alternatively as a legal claim for a violation of Rule 13e-3 and as an equitable claim for a violation of the majority shareholders fiduciary duty): that non-fraudulent, material omissions concerning the "fairness" of the cash out price were made in the proxy statement. Because plaintiffs do not claim in the briefs on appeal that Nationwide Mutual, the majority shareholder, failed to disclose specific information other than that required by Rule 13e-3, we do not reach the question whether, under Ohio law, a majority shareholder has additional disclosure burdens beyond those required by federal law. Accordingly, because of the limited claim plaintiffs make, we expect that proof of material omissions and resulting damages, if applicable, will be similar under either theory (Rule 13e-3 or state law fiduciary duty claim). In any event, plaintiffs may recover, if at all, only once because their injury is the same whether they proceed under state or federal law.

We have reviewed all of plaintiffs' claims on appeal and conclude that the District Court erred in granting summary judgment on plaintiffs' Rule 13e-3 claim, as described above, and on plaintiffs' claim under Ohio law that Nationwide Mutual breached its fiduciary duty as

majority shareholder to disclose the information specified under Item 8 of Rule 13e-3. Accordingly, to this extent, the judgment of the District Court is reversed and the case remanded for trial on the two remaining issues.

RALPH B. GUY, JR., Circuit Judge, dissenting. I believe that the district court judge properly analyzed the issues in this case and found them appropriate for disposition by summary judgment. I would affirm on the basis of the district court's opinion.

IN THE UNITED STATES COURT OF APPEALS
FOR THE SIXTH CIRCUIT

Case No. 89-4084

HOWING CO., *et al.*,
Plaintiffs-Appellants,

v.

NATIONWIDE CORPORATION, *et al.*,
Defendants-Appellees.

Appeal from the United States District Court
for the Southern District of Ohio, Western Division

MOTION OF DEFENDANTS-APPELLEES NATIONWIDE CORPORATION AND NATIONWIDE MUTUAL INSURANCE COMPANY FOR STAY OF MANDATE PENDING APPLICATION FOR WRIT OF CERTIORARI AND MEMORANDUM IN SUPPORT THEREOF

MOTION GRANTED

April 16, 1991

Entered by the Clerk pursuant to Rule (8B) Sixth Cir. Rules. /s/ Leonard Green, Clerk

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Dated: March 25, 1991

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF OHIO
WESTERN DIVISION

C-1-83-1693

HOWING CO., INC., *et al.*,
Plaintiffs,

vs.

NATIONWIDE CORP., *et al.*,
Defendants.

OPINION AND ORDER GRANTING MOTION FOR SUMMARY JUDGMENT

[Filed Nov. 16, 1989]

Spiegel, J.

BACKGROUND

This matter is before the Court on the remand order in *Howing v. Nationwide Corporation*, 826 F.2d 1470 (6th Cir. 1987), *cert. denied*, 108 S. Ct. 1008 (1988). Originally, this action challenged the legality and fairness of a cash-out merger by a majority shareholder, Nationwide Mutual Insurance Corporation, for the stock of Nationwide Corporation. Specifically, the plaintiffs challenged a 1982 Nationwide Corporation proxy statement under multiple federal securities laws and regulations as well as the common law of Ohio.

We granted summary judgment for the defendants on all of plaintiffs' claims and, on appeal, the Court of Appeals affirmed the dismissal of all but one of plaintiffs'

securities law claims, narrowing the federal case to one remaining point. The Sixth Circuit held that the Nationwide Corporation's proxy statement violated certain disclosure requirements of Rule 13e-3, 17 C.F.R. § 240 and Schedule 13E-3 issued thereunder, stating:

> The most serious problem in defendants' proxy statement concerns Item 8(b) compliance. Our review of the proxy statement indicates that defendants have made precisely the kind of conclusory statements prohibited by the Rule. In describing the fairness of the transaction as required by [Schedule 13E-3] Item 8(b), defendants have done nothing more than provide a laundry list of factors considered by their investment banker.
>
> This kind of non-specific disclosure runs counter not only to the SEC's position taken in the Commission release discussed above but also to the Instructions to Item 8(b) of Schedule 13E-3. The Instruction states that the issuer shall "[d]iscuss in reasonable detail the material factors upon which the belief stated in Item 8(a) is based, and to the extent practicable the *weight assigned to each factor*." Thus, the proxy statement is incomplete in that we are not provided with any indication of the weights given the various factors as required by Rule 13e-3, incorporating Schedule 13E-3. Moreover, we therefore have no indication as to whether any of the "sources of value indicate a value higher than the value of the consideration offered to unaffiliated security holders."

Howing v. Nationwide Corp., 826 F.2d at 1478 *quoting from* Exchange Act Release No. 34-17719 at ¶ 17, 245-42 (emphasis in original; footnotes omitted).

Our parent circuit then concluded that the Nationwide proxy statement should have disclosed Nationwide's assessment of book value, liquidation value and going concern value, holding that these "violations of Rule 13e-3,

Item 8 . . . do not constitute 'fraud' . . . but should be considered as violations only of the specific rule in question." *Id.*, 1481 (footnote omitted). The Sixth Circuit issued the following remand order:

> The case is remanded to the District Court with instructions to reconsider defendants' failure to provide Item 8 information in violation of the Rule 13e-3, as established by this opinion. The District Court should also consider issues of materiality of the defendants' omission under Rule 13e-3. After reconsidering the federal claims under Rule 13e-3, the District Court should determine whether it is necessary to decide the alternative state claims respecting breach of fiduciary duty. If so, the District Court's disposition of the state claims should be accompanied by detailed findings of fact and conclusions of law concerning the state standard of fiduciary duty used by the Court.

Id.

Subsequent to the remand, the defendants moved for summary judgment (doc. 131), which is opposed by the plaintiffs (doc. 135), and to which the defendants have replied (doc. 138). We conducted a hearing in this matter on May 30, 1989. The defendants have filed proposed findings of fact and conclusions of law (doc. 132); the plaintiffs have filed a "counterstatement" of findings of fact and conclusions of law (doc. 136). We have carefully considered all of the evidence in the record and the well-articulated arguments of counsel in rendering our decision in this matter. For the following reasons, we conclude that the defendants' motion for summary judgment is well-taken.

PLAINTIFF'S RULE 13e-3 CLAIM

We are persuaded that whether these omissions from the proxy statement were "material" is a threshold question that must be addressed. Previously, we have stated

in this case that for such omissions to support a private cause of action for damages under Rule 13e-3, they must have been material as defined in *TSC Industries, Inc. v. Northway, Inc.*, 426 U.S. 438 (1976). *See Howing v. Nationwide Corp.*, 625 F. Supp. 146, 151 (S.D. Ohio 1985). The *TSC* standard of materiality is as follows:

> An omitted fact is material if there is a substantial likelihood that a reasonable shareholder would consider it important in deciding how to vote. . . . It does not require proof of a substantial likelihood that disclosure of the omitted fact would have caused the reasonable investor to change his vote. What the standard does contemplate is a showing of a substantial likelihood that, under all the circumstances, the omitted fact would have assumed actual significance in the deliberations of the reasonable shareholder.

TSC, 426 U.S. at 449.

In their memorandum in opposition, the plaintiffs discuss in great detail the proxy statement omissions as Rule 13e-3 disclosure violations and seem to urge us to adopt a more stringent materiality analysis for these Rule 13e-3 disclosure violations than the *TSC* standard. They reason that the disclosure requirements under Rule 13e-3 are broader than other SEC disclosure rules because of the coercive nature of going private transactions. *See Howing*, 826 F.2d at 1476 *citing Radol v. Thomas*, 772 F.2d 244, 255 (6th Cir. 1985) *cert. denied*, 106 S. Ct. 3272 (1986). Thus, if the materiality standard is the same for Rule 13e-3 violations as for the anti-fraud securities claims, then, plaintiffs lament that Rule 13e-3 "adds nothing more to going private transaction than existing requirements." Doc. 135 at 23.

The defendants contend that these disclosure violations do not create a *per se* private cause of action for damages, and that the *TSC* materiality standard, as articulated by this Court in our prior decisions in this matter,

is the proper analysis for a Rule 13e-3 violation. We recognize that Rule 13e-3 requires more extensive disclosure than other SEC rules, *see Howing*, 625 F. Supp. at 151, however, we do not believe that the Commission's broad policy-based disclosure requirements for Rule 13e-3 dictate an abandonment of the *TSC* materiality standard which has been applied to private causes of action based upon various securities law violations. *See, e.g., Flamm v. Eberstadt*, 814 F.2d 1169, 1174 (7th Cir. 1987) ("[w]e have taken the definition [of materiality] in *TSC* as suitable for the term wherever it appears in securities law."), *cert. denied*, 108 S. Ct. 978 (1988). We understand the Sixth Circuit to have left undisturbed our definition of materiality as adapted from *TSC* for Rule 13e-3 matters. Of course, in our prior order we never reached the issue of whether these omissions were material because we concluded that there had been no disclosure violations. *Howing*, 625 F. Supp. at 157. Since the Sixth Circuit ruled that the proxy statement omissions were violations of this Rule, that issue need not be revisited. There would have been no need for the remand if these omissions were *per se* material. Thus, we shall proceed to analyze the omissions in question under the *TSC* standard.

We agree with the defendants that the issue before us is a narrow one; the Item 8(b) information that the defendants' failed to provide related to whether any of the sources of value upon which the defendant and its investment banker relied indicated "a value higher than the value of the consideration offered to unaffiliated security holders." *Howing*, 826 F.2d at 1478. Thus, we are simply to determine whether the omissions identified by the Sixth Circuit—the book value, liquidation value, and going concern value—were material. We also concur with the defendants' position that the remand from the Sixth Circuit only requires this Court to contemplate the materiality of the 8(b) omissions, not 8(a) compli-

ance; thus we must examine the factors which Nationwide Corporation, the issuer, analyzed in determining that it reasonably believed that the proposed merger was fair to the unaffiliated shareholders, not the reasonableness of that belief.[1]

Essentially, the defendants contend that the omissions occasioned by the defendants' conclusory statements in describing the fairness of the going private transaction under Item 8(b) are immaterial as a matter of law because the three alternative valuation methods—book value, liquidation value, and going concern value—yielded prices per share that were all lower than the

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[1] Item 8 of Schedule 13e-3, 17 C.F.R. § 240.13e-100 provides in pertinent part:

> Item 8. *Fairness of the Transaction.*
>
> (a) State whether the issuer . . . filing this schedule reasonably believes that the Rule 13e-3 transaction is fair or unfair to unaffiliated holders.
>
> . . . .
>
> (b) Discuss in reasonable detail the material factors upon which the belief stated in Item 8(a) is based, and to the extent practicable, the weight assigned to each such factor. Such discussion should include an analysis of the extent, if any, to which such belief is based on [instruction (1), below].
>
> *Instructions.* (1) The factors which are important in determining the fairness of a transaction to unaffiliated security holders and the weight, if any, which should be given to them in a particular context will vary. Normally, such factors will include, among others . . . whether the consideration offered to unaffiliated security holders constitutes fair value in relation to:
>
> (i) Current market prices,
>
> (ii) Historical market prices,
>
> (iii) Net book value,
>
> (iv) Going concern value,
>
> (v) Liquidation value,
>
> (vi) The purchase price paid in previous purchases disclosed in Item 1(f) of Schedule 13e-3,
>
> (vii) Any report, opinion, or appraisal described in Item 9
>
> . . . .

proposed merger price of $42.50.[2] Thus, they argue, there is no substantial likelihood that a reasonable shareholder would have considered these lower valuations important in deciding how to vote.

First, defendants point out that a reasonable shareholder could have calculated the book value from the information disclosed in the proxy material. They then argue that a liquidation value was irrelevant because Nationwide Corporation had no "off-balance sheet" assets which could be sold for a price exceeding book value, as it was not carrying any assets at book value which were substantially below fair market value such as real estate. Moreover, the defendants argue that the liquidation value of the Nationwide Corporation would be much less than the $42.50 per share offered because New York insurance restrictions effectively "froze" more than half of the value of total shareholders' equity ($260 million out of $462.2 million) that could be distributed in a liquidation.[3] As

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[2] Nationwide affidavits and exhibits show the following:

(1) Book value for Nationwide Corp. is calculated by dividing the shareholders equity ($426,214,000) by the number of outstanding common shares (10,284,030), which yields a book value of $41.44 per share.

(2) An exact liquidation value has not been ascertained by Nationwide, however for reasons discussed *infra* at 8-9, Nationwide states that liquidation value would have been considerably less than book value because the whole was considered more valuable than the sum of the parts.

(3) Going concern value, likewise, is not easily calculable with mathematical precision; one accepted method of calculating going concern value multiplies the company's income over the preceding five years times a multiplier based on price-to-earnings ratios of comparable companies. Applying this formula to Nationwide, the going concern value is $20.80 ($3.27 per share average Nationwide earning over past five years x 6.36 comparable company multiplier).

[3] Under N.Y. Insurance Law § 4231(f)(2)(B), Nationwide Corporation sold both "participating" and "non-participating" policies (82% participating), thus, could distribute no profits on partici-

Nationwide is one of the few insurance companies whose profits were so encumbered because of its unique structure and sales practices. Nationwide argues that liquidation value was insignificant because liquidation would have been so impracticable.

An additional factor bearing on the liquidation value is a piecemeal sale is that Nationwide did not have its own force of insurance agents but sold its policies through captive agents who are associated with two affiliated companies, Nationwide Mutual and Nationwide Mutual Fire. Since these agents made most of their income from selling the mutual companies' policies, if Nationwide Corporation was liquidated or sold in pieces, said agents would have retained their associations with the mutual companies rather than going with Nationwide. Thus, Nationwide concluded that the whole entity was considerably more valuable than its pieces.

Finally, defendants contend that the going concern value was below both book value and the proposed merger price for similar reasons that liquidation value would be less than book value or the merger price, *i.e.*, Nationwide's lack of sales force and the State restrictions on distribution of profits stigmatized it as an investment, thus lowering its going concern value.

In response, the plaintiffs argue that the reasonableness of the issuer's belief as to the fairness of the merger must be considered on remand and that reasonableness is a question of fact which precludes the granting of summary judgment in favor of the defendants. Their experts have concluded that the cash merger price of $42.50 was unfair, concluding that their calculation of the book value, liquidation value, and going concern value yielded values in excess of $42.50; they disagree with the defendants'

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pating policies in excess of the greater of either ten percent of such profits or fifty cents per thousand dollars of participating life insurance in force for the benefit of the shareholders.

conclusions as to the impact of New York insurance law on either liquidation or going concern value. Plaintiffs argue that there are factual issues as to what decision-making processes took place in arriving at the $42.50 price as well as the reasonableness of the same and that even if the defendants had determined that these valuations were insignificant, nevertheless, they should have been fully discussed in the proxy statement.

The plaintiffs also take the position that whether these omissions were material poses mixed questions of law and fact which are inappropriate for summary judgment disposition, *citing TSC*, 426 U.S. at 450. We note, however, that the *TSC* Court stated that summary judgment is appropriate where the evidence is such that reasonable minds could not differ on the question of the materiality of the particular omissions. *Id.*

The narrow question that we must decide on a motion for summary judgment is whether there is "no genuine issues as to any material fact and [whether] the moving party is entitled to judgment as a matter of law." Rule 56(c), Fed. R. Civ. P. The Court cannot try issues of fact on a Rule 56 motion, but is empowered to determine only whether there are issues to be tried. *In re Atlas Concrete Pipe, Inc.*, 668 F.2d 905, 908 (6th Cir. 1982). The moving party "has the burden of showing *conclusively* that there exists no genuine issues as to a material fact and the evidence together with all inferences to be drawn therefrom must be read in the light most favorable to the party opposing the motion." *Smith v. Hudson*, 600 F.2d 60, 63 (6th Cir.) (emphasis original), *cert. denied*, 444 U.S. 986 (1979). And, "while the movant's papers are to be closely scrutinized, those of the opponent are to be viewed indulgently." *Id.* at 63. "[T]he District Court [is] obligated to consider not only the materials specifically offered in support of the motion, but also all 'pleadings, depositions, answers to interrogatories, and admissions' properly on file and thus properly before

[the] court." *Id.*, quoting Rule 56(c), Fed. R. Civ. P. Summary judgment "must be used only with extreme caution for it operates to deny a litigant his day in court." *Id.* We are further guided by the Supreme Court's recent elaboration of this standard in *Celotex Corporation v. Catrett*, 477 U.S. 317 (1986) as follows:

> . . . the plain language of Rule 56(c) mandates the entry of summary judgment, after adequate time for discovery and upon motion, against a party who fails to make a showing sufficient to establish the existence of an element essential to that party's case and on which that party will bear the burden of proof at trial . . .

477 U.S. at 322.

Accordingly, we have reviewed the evidence in this case to determine if the omissions from the 1982 Nationwide proxy statement would have caused a reasonable shareholder to consider the omitted information important in deciding how to vote. We do not believe that plaintiffs' expert's opinion that book, liquidation, and going concern values should have yielded higher values than the $42.50 offered creates an issue of material fact because Item 8(b) pertains to the factors that the issuer, not someone else, considered important in determining the fairness of the going private transaction. Moreover, disputes as to the substantive fairness of the price offered shareholders in this transaction cannot be the subject of our inquiry on plaintiffs' federal claim as federal securities law concerns disclosure questions, not the terms of a transaction. *See generally, Santa Fe Industries, Inc. v. Green*, 430 U.S. 462, 477-78 (1977); *Nash v. Farmers New World Life Ins. Co.*, 570 F.2d 558, 562 (6th Cir.), *cert. denied*, 439 U.S. 822 (1978).

We observe that while the parties dispute the legal conclusions to be drawn from the facts surrounding the Nationwide going private transaction, there are no genuine disputes about the facts, themselves. Since the

omitted facts, the book value, the liquidation value, and the going concern value developed by the defendants all resulted in amounts less than the cash out price of $42.50, we conclude that having such information would not have significantly altered the "total mix" of information available to the shareholders in deciding how to vote on the merger issue. *See TSC*, 426 U.S. at 449. Thus, because reasonable minds could not differ that these omissions were immaterial, summary judgment shall be entered in favor of the defendants on plaintiffs' federal securities claim under Rule 13e-3.

PLAINTIFFS' STATE CLAIMS

The remand order also provided that after we decide the plaintiffs' federal claim, this Court should then determine whether it is necessary to decide the alternative state claims respecting breach of fiduciary duty, and, if so, to provide findings of fact and conclusions of law upon which we based our decision. For the following reasons, we conclude that our prior holding need not be reconsidered; defendants are entitled to summary judgment on plaintiffs' state claims as well, thus, these claims must also be dismissed. The following are our findings of fact and conclusions of law.

Findings of Fact

In October of 1982, the president of Nationwide Corporation, John L. Marakas, learned that Nationwide Mutual Insurance Company, the owner of approximately 82% of Nationwide Corporation's stock as of November 1982, had decided to formally consider a merger with the Corporation. Marakas notified the two outside members of the Corporation's Executive Committee, members who were not employees of the Corporation nor directors or employees of Nationwide Mutual, of the possible merger and that the Corporation had hired the First

Boston Corporation, a large and respected investment banker, to represent the interests of the public stockholders in determining a fair price for the public shares.

First Boston was given complete discretion to set a price which it thought was fair. It formed a team of six experts to study the value of Nationwide Corporation. Employees of the Corporation were directed to provide any financial data or records that First Boston needed for its study. First Boston followed its standard procedures for determining a fair price; it studied projections for 1982 and 1983 earnings and interviewed numerous officers of the Corporation. This six-member team then produced a report containing its data and conclusions, which report was given to six other persons in various departments of First Boston for a review as to the objectivity and thoroughness of the team's data and conclusions. All twelve met twice for oral presentation and critique of the report.

The First Boston study of Nationwide Corporation's value was completed in late October 1982. It recommended a price of $42.50 per share, a 67% premium over the market price of $25-$26 at that time, as fair to the public stockholders. First Boston determined that the $42.50 price exceeded the price ascertained by three alternative valuation methods. Book value, easily calculated from proxy materials (shareholders equity divided by outstanding shares) was $41.44 per share. Liquidation value was less than book value because the corporation was more valuable as a whole than the sum of its parts due to the lack of its own sales force, its lack of undervalued assets, and because over half of the equity which would normally be distributed to shareholders upon liquidation was "frozen" by operation of New York Insurance law.[4] Going concern value, calculated by multiplying the average price/earnings ratio of comparable companies

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[4] New York Insurance Law § 4231(f)(2)(B) (McKinney 1985).

(6.36) times the Corporation's average earnings per share over for the preceding five years ($3.27) was $20.80.[5]

Meanwhile, the law firm of Bricker & Eckler was retained by the Executive Committee to negotiate the terms of the merger agreement with Nationwide Mutual on behalf of the public stockholders. Bricker & Eckler obtained three provisions to safeguard the interests of the public stockholders. One was to permit the merger to be aborted if First Boston withdrew its opinion that the price of $42.50 was fair. Under the second provision, the Class A directors, all of whom were independent of Nationwide Mutual, would have the authority to cancel the merger if a majority of the public shareholders did not vote in favor of it. The third provision allowed the merger to be halted if a third party offered to purchase the publicly held shares at a higher price.

At its November 2, 1982 meeting, the Nationwide Corporation Board was advised that Nationwide Mutual was on the verge of making its merger proposal. Representatives of Nationwide Mutual outlined the anticipated structure of the proposal. The Board voted to create an Evaluation Committee comprised of the five independent outside directors of the Corporation. None of these people was employed by the Corporation or Nationwide Mutual or had any connection with either entity other than serving as directors of Nationwide Corporation. None had any financial interest in the transaction other than being holders of Class A common stock.

This Evaluation Committee met following the adjournment of the full Board meeting and discussed the pro-

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[5] Officers of Nationwide Mutual considered $42.50 to be in excess of the fair market value of the Corporation, yet its Investment Committee voted unanimously to recommend to the full board to make a merger proposal at that price. The president of Nationwide Corporation also considered this price to be in excess of the price that he would recommend as fair, a range of from $36-$39.

posed merger for the rest of the day. The Evaluation Committee exercised the authority given it by the Board to retain counsel; Bricker & Eckler served as counsel, just as it had in negotiating the merger, and participated in the remainder of the Evaluation Committee meeting. The Evaluation Committee met with three representatives of First Boston and questioned them about the firm's expertise in the valuation of companies in going private transactions and specifically inquired into whether First Boston had exercised independent professional judgment in making its recommendation. To this end, members posed twenty questions, which had been prepared by the independent counsel, to First Boston such as whether the Corporation or Nationwide Mutual had restricted access to information (they had not) or whether the Corporation or Nationwide Mutual had suggested any price range (they had not). The Evaluation Committee concluded that First Boston had represented the interests of the public stockholders of the Corporation in arriving at a fair price for their stock. The First Boston report was reviewed in detail; numerous members and counsel asked questions pertaining to the soundness of First Boston's methodology and conclusions.

The Evaluation Committee concluded that it was proper to rely on First Boston's valuation of the Corporation and that the recommended price of $42.50 per share was fair; no member of the Committee, nor counsel, disagreed with First Boston's conclusion that alternative valuation methods—book value, liquidation value, going concern value—yielded prices below $42.50. The Evaluation Committee unanimously voted to recommend merger to the full Board at the recommended price of $42.50 based upon the expertise of First Boston and the thoroughness of its analysis of the proposed merger.

The next day, November 3, 1982, the full Board of Nationwide Corporation met to consider the proposed merger. Six of the eleven directors present were un-

affiliated with Nationwide Mutual. At this meeting, the Evaluation Committee presented its conclusions and the bases for them. Representatives of First Boston were present and were questioned about the factors underlying its recommended price per share. Based on the presentations of the Evaluation Committee and First Boston, the directors determined that $42.50 per share was a fair price for the publicly held shares, having considered alternative valuations. The Board then unanimously voted to adopt the draft merger agreement containing the three provisions submitted by Bricker & Eckler to safeguard the interests of the public shareholders.

The proposed merger and the Board's recommendation in support thereof were announced on November 3, 1982. The merger price of $42.50 represented a premium of 52% over the bid price for Nationwide Corporation Class A stock of $28 per share the day before the announcement. Over the next month, the price increased to approximately $40 per share in anticipation of the proposed merger.

On December 9, 1982, proxy materials were sent to all Nationwide Corporation shareholders describing the proposed merger. The proxy statement contained information about the Corporation and its subsidiaries and affiliations with other Nationwide companies; it described Corporation operations and contained twenty pages of financial information. The proxy statement advised that the proposed merger would be subject of a stockholder vote at a meeting to be held January 18, 1983. 94.7% of the publicly held shares that took part in the voting voted in favor of the merger and a majority of all publicly held shares voted in favor of the proposed merger. The named plaintiffs did not vote.

Conclusions of Law

We recognize that the plaintiffs have not sought the relief of appraisal under Ohio Revised Code § 1701.85 as

dissenting shareholders to the merger;[6] the plaintiffs contend, and we agree, that such appraisal proceedings are not the exclusive remedy available to shareholders when it is claimed that such merger constituted a breach of fiduciary duty. The distinction between causes of action and remedies available to shareholders who challenge a merger has been noted by Judge Rubin:

> Section 1701.85(A)(1) says "A shareholder . . . is entitled to relief *as a dissenting shareholder* . . . only in compliance with this section." (emphasis in original) with respect to the above claims for breach of duty against the Marathon defendants, plaintiffs are not seeking relief as *dissenting* shareholders, i.e., shareholders dissatisfied with the outcome of the merger vote. Rather, they are seeking relief simply as shareholders of Marathon, a company whose directors, they allege, breached their duty to *all* shareholders by negotiating and approving a transaction which was, allegedly, inherently unfair. Under this theory, plaintiffs status with respect to the merger vote is irrelevant. Since these breach of fiduciary duty claims do not rest on plaintiffs' status as dissenting shareholders, the remedy of § 1701.85 is not exclusive.

Radol v. Thomas, C-1-82-13, slip op. at 16-17 (S.D. Ohio, May 16, 1983).

It is questionable whether plaintiffs have stated a cause of action for breach of fiduciary duty against Nationwide Corporation because the corporation did not owe a duty to its stockholders and its directors are not parties to this

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[6] There is no dispute that in Ohio appraisal is a dissenting shareholder's exclusive remedy for challenging the validity of a merger unless the merger is fraudulent, ultra vires, or not authorized by statute. *See Radol v. Thomas*, C-1-82-83, slip op. at 15-16 (S.D. Ohio, May 16, 1983); Ohio Rev. Code § 1701.85. Here we find no evidence that the merger was fraudulent, ultra vires, or not authorized by statute.

litigation. *See Radol v. Thomas*, 772 F.2d 244, 257-58 (6th Cir. 1985), *cert. denied*, 477 U.S. 903 (1986). Nevertheless, we shall consider if Nationwide Corporation, through its directors, breached any duty to the plaintiffs. Since the merger was unanimously approved by directors of Nationwide Corporation, a majority of whom were disinterested, the transaction is governed by the business judgment rule. *Radol*, 772 F.2d at 257-58. Under the business judgment rule, actions are presumed to be taken on an informed basis and in good faith belief that they are in the best interests of the company. *Cottle v. Storer Communications, Inc.*, 849 F.2d 570, 575 (11th Cir. 1988) (interpreting Ohio law). *See generally* Ohio Revised Code § 1701.59. At no time did Nationwide Corporation suggest a price or a range of prices per share. Indeed, it is evident that disinterested Board members, as members of the Executive and Evaluation Committees, who were advised throughout by independent counsel, carefully considered the fairness of the proposed merger from the outset when they were first notified of the proposed merger; they retained independent counsel who negotiated with Nationwide Mutual to obtain provisions in the merger agreement protecting the public stockholders. The retained financial consultant, First Boston, represented the interests of the public stockholders and had free access to Corporation information in evaluating the company. First Boston spent nearly a month in finalizing its conclusions and recommended price per share. The Evaluation Committee, comprised of five independent, outside Board members unanimously approved the merger after careful scrutiny of the First Boston study. In turn, based upon the report of the Evaluation Committee and its own review of the First Boston study, the full Board unanimously voted in favor of the merger. We conclude, therefore, that under the business judgment rule, the presumption that the action was taken on an informed basis, and in the good faith belief that the action was in the best interest of the company has not been rebutted. *Compare Edelman v. Frue-*

hauf Corp., 798 F.2d 882, 885-86 (6th Cir. 1986) (board committee's mere "rubber stamp" of proposal submitted by management rebuts business judgment rule) *with Rosenblatt v. Getty Oil Corp.*, 493 A.2d 929, 939 (Del. 1985) (Board decision was informed one where directors were briefed by financial advisor and legal counsel, where they met with substantial shareholder threatening litigation, and where transaction was approved by a majority of disinterested directors).

Here, plaintiffs have apparently sued Nationwide Mutual for using its position as dominant shareholder of Nationwide Corporation to structure and propose a freeze out merger which, plaintiffs claim, is grossly unfair to the minority. However, we observe that the price to be paid for the shares was not one dictated by Nationwide Mutual, as dominant shareholder of Nationwide Corporation, but was arrived at by an independent investment banker representing the interests of the public stockholders which stockholders were also represented by an independent law firm. We conclude that the merger was fair, as the evidence shows extraordinary steps taken to safeguard the interests of the public shareholders as evidenced by the unanimous approval by the Board, a majority of whom were disinterested and the overwhelming approval by the public stockholders. *See Rosenblatt*, 493 A.2d at 939; *see also Armstrong v. Marathon Oil Co.*, 32 Ohio St. 3d 397, 421, 513 N.E.2d 776, 797 (1987) (acknowledging that under some circumstances, a breach of fiduciary duty claim, distinct from appraisal, may be raised against controlling shareholders); Ohio Revised Code § 1701.60. We know of no authority which suggests that Nationwide Mutual's mere acceptance of a price set by an independent investment banker could conceivably constitute a breach of its fiduciary duty toward the minority shareholders. *Cf. Weinberger v. UOP, Inc.*, 457 A.2d 701 (Del. 1983). Thus, we conclude that whatever fiduciary duty Nationwide Mutual had for the plaintiffs was not breached.

CONCLUSION

For the foregoing reasons, we conclude on remand that the facts omitted from Item 8(b) of Schedule 13E-3 were not material, as there was no substantial likelihood that a reasonable shareholder would have considered them important in deciding how to vote as such information would have disclosed that the book value, liquidation value, and going concern value of Nationwide Corporation were all less than the cash out price of $42.50. Therefore, the defendants' motion for summary judgment on the remaining federal claim is GRANTED.

On remand, we were further instructed to determine whether it was necessary to decide the alternative state claim respecting a breach of fiduciary duty. We recognize that the plaintiffs are not limited to the statutory appraisal remedy that pertains only to dissenting shareholders' challenges of a merger. Here, the plaintiffs have attempted to raise a breach of fiduciary duty claim against either or both Nationwide Corporation and Nationwide Mutual. Our analysis of the facts and the law disclose that there was no breach of any fiduciary duty. Accordingly, for the foregoing reasons contained in our Findings of Fact and Conclusions of Law, we reaffirm our decision dismissing plaintiffs' state claims.

This action is hereby dismissed.

SO ORDERED.

/s/ S. Arthur Spiegel
S. ARTHUR SPIEGEL
United States District Judge

UNITED STATES COURT OF APPEALS
FOR THE SIXTH CIRCUIT

No. 85-3929

HOWING CO., *et al.*,
Plaintiffs-Appellants,

v.

NATIONWIDE CORPORATION, *et al.*,
Defendants-Appellees.

Argued Oct. 2, 1986

Decided Aug. 7, 1987

William R. Jacobs argued, Strauss, Troy & Ruehlmann Co., L.P.A., Cincinnati, Ohio, for plaintiffs-appellants.

Jeffrey S. Davidson argued, Washington, D.C., for defendants-appellees.

Before MERRITT, GUY and NORRIS, Circuit Judges.

MERRITT, Circuit Judge.

Under § 13(e) of the Securities Exchange Act of 1934, a Williams Act provision enacted in 1968, a company that has issued publicly traded stock is prohibited from buying it back unless the issuer complies with rules promulgated by the SEC.[1] This appeal raises issues concerning the

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[1] *See* 15 U.S.C. § 78m(e)(1) (1982) which authorizes the Securities and Exchange Commission in the going private context, to adopt rules and regulations "(A) to define acts and practices which

existence of a private right of action under § 13e-3, the nature of the disclosure duty imposed by Rule 13e-3,[2] and the interrelationship of this provision with other antifraud rules.

Pursuant to its authority under § 13e-3, the SEC has issued Rule 13e-3 and Schedule 13e-3, a long and detailed set of disclosure requirements governing such "going private" transactions. Schedule 13e-3 accompanying the Rule requires that numerous items of information about the transaction be filed with the Commission, including three items pertinent to this case, i.e., Items 7, 8 and 9. Item 7 covers the "reasons" for the transaction; Item 8 requires a statement concerning the fairness of the transaction; and Item 9 requires disclosure of appraisals and other information concerning the value of the stock. The Rule also provides that this same information be disclosed to the selling shareholders.

The basic questions presented in this case are: (1) whether the plaintiffs have a private right of action under § 13e-3 to police non-compliance with Rule 13e-3; (2) and if so, whether the disclosure requirements of Rule 13e-3 have been met; and (3) if those requirements have not been met, whether defendant's conduct in violating Rule 13e-3 also gives rise to liability under the antifraud provisions of Rules 10b-5 and 14a-9.

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are fraudulent, deceptive, or manipulative, and (B) to prescribe means reasonably designed to prevent such acts and practices." This section provides further that "[s]uch rules and regulations may require such issuer to provide holders of equity securities of such class with such information relating to the reasons for such purpose, the source of funds, the number of shares to be purchased, the price to be paid for such securities, the method of purchase, and such additional information, as the Commission deems necessary or appropriate in the public interest or for the protection of investors . . . ."

[2] 17 C.F.R. § 240.13e-3.

Parties and Summary of Disposition Below

Defendant Nationwide Corporation is one of the largest life insurance holding companies in the United States. Originally incorporated in 1947 as Service Insurance Agency, the company has enjoyed steady growth since its affiliation with the Nationwide group of insurance companies in September 1955. As a result of this affiliation, the company adopted its present name and issued a special class of common stock (Class B common) which was held entirely by two Nationwide companies: Nationwide Mutual Insurance Company and Nationwide Mutual Fire Insurance Company. The Class A common stock continued in the hands of individual shareholders.

Because of the way voting rights were allocated between the Class A and Class B stock, complete ownership of the Class B shares gave Nationwide Mutual and Nationwide Mutual Fire effective control of the corporation. The Class B shares were entitled as a class to one-half of the voting power of the corporation as long as the percentage of Class B shares outstanding relative to outstanding shares of all classes combined did not fall below forty percent. Since it appears that the amount of outstanding Class B common was at all times sufficient to meet this threshold, Nationwide Mutual and Nationwide Mutual Fire held the same voting power as all the Class A shares combined. Under these circumstances, it is clear that these companies controlled the corporation despite wide public ownership of the Class A shares.

Nationwide Mutual and Nationwide Mutual Fire began to eliminate public ownership of Nationwide Corporation in December 1978 when these companies made a tender offer to buy the Class A shares for $20.00 per share net in cash. By January 1979, Nationwide Mutual and Nationwide Mutual Fire had purchased 4,074,695 Class A shares through this offer. After the tender offer, Nationwide Mutual and Nationwide Mutual Fire contin-

ued to purchase shares in the open market at prices ranging between $22.50 to $24.62 per share. These Nationwide Mutual Fire ownership of 85.6% of the Class A common stock formerly held by the public.

In November 1982, the Board of Directors of Nationwide Corporation approved a transaction in which Nationwide Mutual and Nationwide Mutual Fire would acquire the remaining Class A shares at $42.50 per share. As a result, Nationwide Corporation would become a wholly-owned subsidiary of the two mutuals, and would have no public ownership. This transaction was approved by 94.7% of the Class A shares. Plaintiffs in the present litigation abstained from voting their shares respecting the merger or seeking their appraisal remedy under state law.

The present class action began with an action by Belle Efros, a Nationwide shareholder, seeking a preliminary injunction with respect to a vote on the proposed merger. Following the denial of the Efros motion for a preliminary injunction, the merger was approved by 94.7% of the voted public shares. The District Court ultimately consolidated the Efros action with an action brought by the Howing Company and Douglas McClellan, two former shareholders of Nationwide. The District Court also later conditionally certified the case as a class action. The final amended complaint in this action raised claims under the Securities Exchange Act of 1934 §§ 10(b), 13(e), and 14(a) and rules promulgated thereunder as well as state law claims based on a breach of fiduciary duty.

The defendants moved for summary judgment and plaintiffs filed a cross-motion for partial summary judgment. The District Court granted defendants' motion, denied plaintiffs' cross-motion, and dismissed the amended complaint, 625 F. Supp. 146 (D. Ohio 1985).

The District Court identified compliance with Rule 13e-3 as the principal issue in the case. The District Court framed its scope of review as follows:

> We therefore will review the proxy material of Nationwide Corporation to see if it meets the standards of disclosure required by Rule 13e-3. If in any instance there has been a failure to meet the standard, we will then examine whether such failure constitutes a material breach, and if we conclude that there is a jury questions concerning the materiality of the breach, then, of course, there would be a genuine issue of fact to be determined.

625 F. Supp. at 151.

In reviewing the proxy statement's compliance with Rule 13e-3, the District Court begins with Item 7 of the Rule which essentially covers the "reasons" for the transaction. The District Court concluded that the proxy statement adequately disclosed the purposes of the transaction as well as its benefits and detriments. The District Court stated that "[w]e decline to second guess the directors of Nationwide as to the stated purpose for the merger," 625 F. Supp. at 152, and stated further that "[w]e conclude that the detriments and benefits were adequately discussed in the proxy statement and that the gravamen of plaintiffs' argument on this issue is actually that the merger price itself was not fair to the public stockholders." *Id.* at 153.

With respect to the proxy statement's compliance with the Item 8 fairness disclosure, the District Court considered three contentions by plaintiffs: (1) the proxy statement did not sufficiently discuss the net book value, liquidation value, and going concern values of Nationwide shares; (2) the proxy statement did not explicitly state that Nationwide stock was "thinly traded"; and (3) the proxy statement did not sufficiently discuss the basis for the First Boston opinion letter.

On the question of valuation, the District Court noted that "the proxy statement contained extensive financial information necessary to compute the net book liquidation, and going concern values of Nationwide shares." 625 F. Supp. at 155. The District Court found that the proxy statement met the requirements of Rule 13e-3 in this regard:

> Rule 13e-3 "merely requires that an opinion be given and the material factors on which it is based be disclosed." We conclude that defendants satisfied this requirement of Rule 13e-3 by listing the factors considered by the Evaluation Committee and by candidly stating that no specific weight was given to any one factor, but of particular importance in the consideration was First Boston's opinion and the fact that the merger price represented a premium over the market price of the stock.

Id.

With respect to the "thinly traded" nature of the stock, the District Court found that sufficient information was disclosed "to allow a reasonably prudent shareholder to make his own characterization of the market for the Nationwide stock." *Id.* at 156. Specifically, the District Court noted that the proxy statement disclosed that "Nationwide Mutual owned 85.6% of the outstanding Class A shares, the number of publicly held shares, and that the stock was traded only in the 'over-the-counter market.'" *Id.* at 155-56.

Concerning the proxy statement's discussion of the First Boston opinions, the District Court addresses plaintiffs' contention that the proxy statement failed to set forth projected growth rates and increase of earnings. Relying on this Court's reasoning in *Starkman v. Marathon*, 772 F.2d 231 (6th Cir. 1985), the District Court considered the omitted information to be "soft" information since "earnings and cash flow projections do not rise to the level of substantial certainty triggering a duty to

disclose." 625 F. Supp. at 156 (citing *Starkman*, 772 F.2d at 242). Accordingly, the District Court concluded that defendants were not required to disclose projected growth rates and future increase of earnings.

The District Court also dismissed plaintiffs' argument that the First Boston opinion "should have disclosed information regarding comparable life insurance companies as such information would reveal the unfairness of the cash out price." 625 F. Supp. at 157. The District Court rejected plaintiffs' argument on the following grounds: "There is no indication that there was anyone or any other entity, besides Mutual, interested in purchasing Nationwide. Therefore, the alleged omission of 'comparable values' was immaterial and indeed such information may have been misleading if discussed." *Id.*

The District Court concluded overall that the proxy statement satisfied the requirements of Rule 13e-3. The District Court stated:

> Most important, there was sufficient information disclosed in the proxy statement to enable the stockholders to make an informed decision on what to do. It is the conclusion of the Court, therefore, that there is no genuine issue of material fact concerning the adequacy of the proxy statement when measured against the standards set forth in Rule 13e-3, and that any omissions pointed out by plaintiffs were not material as defined by the Court in *TSC Industries, Inc.* [*Northway Inc.*], 426 U.S. [438] at 449, 96 S.Ct. [2126] at 2132 [48 L.Ed.2d 757 (1976)].

Id.

Finally, the District Court considered and rejected plaintiffs' state law claims. The District Court stated that "since there is no evidence of any breach of fiduciary duty owed plaintiffs by defendants, and the merger was neither unauthorized by statute, illegal nor ultra vires under Ohio corporation law, the Ohio statu-

tory appraisal right constituted plaintiffs' exclusive state law remedy." *Id.* The District Court noted that plaintiffs failed to resort to the appraisal remedy.

Private Right of Action Under § 13(e)

In the present case, we must decide a question of first impression in the federal courts of appeals: Does § 13(e) of the Securities and Exchange Act of 1934 allow a private right of action for damages? The District Court assumed that a private right of action exists, and we agree. Based upon our review of the statute, the legislative history, and the Supreme Court's decisions respecting private rights of action, we conclude that such a right of action does exist under § 13(e).[3]

The law relating to judicially-implied private rights of action under federal statutes has undergone a process of evolution over the past seventy years. When federal lawmaking was a less detailed and comprehensive endeavor, a private remedy was ordinarily presumed in favor of the class for whose benefit the statute was enacted. *See Merrill Lynch, Pierce, Fenner & Smith v. Curran*, 456 U.S. 353, 374-75, 102 S. Ct. 1825, 1837-38, 72 L. Ed. 2d 182 (1982) (citing *Texas & Pacific Ry. Co. v. Rigsby*, 241 U.S. 33, 36 S. Ct. 482, 60 L. Ed. 874 (1916)). As the complexity of federal legislation and volume of litigation increased, the liberal *Rigsby* rule became unworkable. A unanimous Supreme Court responded by modifying the law or implied private rights of action. The result, announced in *Cort v. Ash*, 422 U.S. 66, 95 S. Ct. 2080, 45 L. Ed. 2d 26 (1975), was a four-part test that focused

[3] Two District Courts have split on the existence of a private right of action under § 13(e). *See Fisher v. Plessey Co.*, [1982-83 transfer binder] Fed.Sec.L.Rep. (CCH) ¶ 99,246 (S.D.N.Y. June 22, 1983) [Available on WESTLAW, DCT database] (implying private action). *But see Kalmanovitz v. G. Heileman Brewing Co.*, 595 F. Supp. 1385 (D. Del. 1984) (denying right of action), *aff'd on other grounds*, 769 F.2d 152 (3d Cir. 1985). For a discussion of the error in the *Kalmanovitz* reasoning, see note 4 *infra*.

primarily on congressional intent. Under *Cort*, a private right of action exists where: (1) the plaintiff is a member of the class for whose especial benefit the statute was enacted; (2) there is any indication, explicit or implicit, of legislative intent to support such a remedy; (3) an implied private right of action is consistent with the purposes of the legislative scheme; and (4) the cause of action is not "one traditionally relegated to state law, in an area basically the concern of the states, so that it would be inappropriate to infer a cause of action based solely on federal law." *Id.* at 78, 95 S. Ct. at 2088 (citations omitted).

This decision and those following it, such as *Cannon v. University of Chicago*, 441 U.S. 677, 99 S. Ct. 1046, 60 L. Ed. 2d 560 (1979), were intended to suggest that Congress be more explicit about private remedies in future legislation. However, because the rule announced by *Cort* was such a departure from existing law, there has been some reluctance to apply it to legislation enacted prior to that decision. According to *Cannon*, Congress is entitled to rely on the "contemporary legal context" in which it acts, 441 U.S. at 698-99, S. Ct. at 1958. When Congress passed legislation prior to *Cort*, that context would presume a private remedy if the statute and its history were otherwise silent. *See Curran*, 456 U.S. at 374-75, 382 n.66, 102 S. Ct. at 1837-38, 1841 n.66.

The decision in *Cannon v. University of Chicago* is particularly instructive. In that case, the Supreme Court held that Congress indicated its intent to allow a private right of action to enforce Title IX of the Education Amendments of 1972 when it patterned that law on another statute—Title VI of the Civil Rights Act of 1964—which had been interpreted to support private suits. Although the *Cort* test was still applied, this adoption theory satisfied the crucial legislative intent test contained in the second *Cort* factor. Given a contemporary legal context in which Title VI had been construed to support a private cause of action, Congress' choice to pattern Title

IX after that previous statute made it "not only appropriate but also realistic to presume that Congress was familiar with these unusually important precedents . . . and that it expected its enactment to be interpreted in conformity with them." *Cannon*, 441 U.S. at 699, 99 S. Ct. at 1958.

In order to determine the existence of a private right of action under § 13(e), therefore, we must apply the criteria established by *Cort v. Ash* with consideration for the "contemporary legal context" in which the legislation was passed. Such an undertaking requires that we under stand the history and the structure of the statute in question.

Section 13(e)(1) of the Securities Exchange Act was not part of the original statute but was added by the Williams Act in 1968. The stated purpose of the Williams Act was to protect investors from potential manipulation of tender offers and corporate repurchases of stock. *See Piper v. Chris-Craft Indus.*, 430 U.S. 1, 26-35, 97 S. Ct. 926, 941-46, 51 L. Ed. 2d 124 (1977). The legislation was explicitly patterned after the statutes and regulations then governing proxy solicitations. *See* 113 *Cong. Rec.* 24,665 (1967) (statement of Senator Williams). As a result, the language of § 13(e) and other Williams Act provisions parallel that used in § 14(a) of the Securities Exchange Act of 1934.

From this legislative history, it is clear that the first three *Cort* factors are satisfied with respect to § 13(e). The first *Cort* factor applies the old *Rigsby* test and asks if the plaintiff is one for whose especial benefit the statute was enacted. Since the Supreme Court established in *Piper* that the Williams Act was intended "for the protection of investors," 430 U.S. at 35, 97 S. Ct. at 946, it cannot be gainsaid that the investors such as the current plaintiffs fall within the benefitted class. Thus, the first *Cort* factor is met.

The second *Cort* factor—whether there is evidence of a legislative intent to allow or deny a private remedy—favors a private cause of action for two distinct reasons. First, since the Williams Act was explicitly patterned on the proxy rules, the analysis employed by the Supreme Court in *Cannon v. University of Chicago* applies here. When § 13(e) was adopted in 1967, the Supreme Court had already recognized an implied private right of action under § 14(a) in *J.I. Case v. Borak*, 377 U.S. 426, 84 S. Ct. 1555, 12 L. Ed. 2d 423 (1964). In support of the private action upheld in *Borak*, Justice Clark, speaking for the Court, placed special emphasis on the power granted to the SEC "to protect investors." *Id.* at 432, 84 S. Ct. at 1559. Under the rationale of *Cannon*, therefore, Congress indicated its desire to allow a private right of action under § 13(e) when it chose language that was identical to the crucial language supporting a private right of action under § 14(a). *See also Lorillard v. Pons*, 434 U.S. 575, 580-81, 98 S. Ct. 866, 870, 55 L. Ed. 2d 40 (1978) (Congress presumed to incorporate interpretations of prior law when it incorporates text into new law).

Aside from Congress' choice of § 14(a) as a model, there is a second aspect of the "contemporary legal context" which supports a private right of action for § 13(e). At the time the Williams Act was passed, implied rights of action were in a heyday of sorts. *See Cannon*, 441 U.S. at 718, 99 S. Ct. at 1968 (Rehnquist, J., concurring); *Leist v. Simplot*, 638 F.2d 283, 316-17 (2d Cir. 1980). Congress could have justifiably presumed that its silence with regard to private actions would be interpreted to indicate authorization. Silence, in the contemporary legal context of the Williams Act, did not constitute disapproval of an implied private action. Since there is no evidence of legislative intent to deny a private remedy, Congress' choice to incorporate the proxy rules without additional comment is an indication of legislative intent sufficient to satisfy the second *Cort* test. *See Cannon*, 441

U.S. at 698-99, 99 S. Ct. at 1958-59; *Cort*, 422 U.S. at 82, 95 S. Ct. at 2089.

The third element of the *Cort* test—where an implied private action is consistent with the legislative scheme—is also satisfied by § 13(e). Although the statute is designed for the protection of investors, no mechanism is provided by which these investors can vindicate their interests.[4] As noted by Justice Clark in *Borak* with respect to the proxy rules, private enforcement may be the *only* way to achieve the purposes of § 13(e) given limited resources under the SEC's command. *Borak*, 377 U.S. at 433, 84 S. Ct. at 1560. Under these circumstances, "it is the duty of the courts to be alert to provide such remedies as are necessary to make effective . . . congressional purpose." *Id.* Since a private right of action would fill a void in enforcement, it is entirely consistent with the legislative scheme established by § 13(e).

The fourth *Cort* factor concerns whether the cause of action is one traditionally relegated to state law. Since 1933, the obligations of an issuer to the public and its stockholders have been a matter of federal law. The specific disclosure duty at issue here is a federal law. In light of the inherently federal nature of this claim, it is clear that a private right of action would not interfere with the regulatory prerogatives of the various states. It is also clear that the plaintiffs in this case meet the requirements set forth by *Cort v. Ash* and its progeny, and are therefore entitled to maintain a private action against Nationwide for violations of § 13(e).

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[4] Section 18 of the Securities Exchange Act, 15 U.S.C. § 78r, provides an express remedy for some subsections of § 13, but not subsection (e). This remedy was provided prior to the Williams Act for misstatements in filings with the Commission. It does not apply where inadequate disclosure is made to shareholders. The critical error committed by the District Court in *Kalmanovitz v. G. Heileman Brewing Co.*, 595 F. Supp. 1385, 1393-95, is the assumption that the § 18 remedy affords relief for aggrieved shareholders.

Rule 13e-3 Compliance

Going private transactions raise unique problems because of their inherently coercive nature: minority shareholders are forced to exchange their shares for cash or other consideration. The coercive effect of these transactions is reinforced by the fact that the majority shareholders control the timing and terms of the transaction.

In promulgating Rule 13e-3 pursuant to § 13(e), 17 C.F.R. § 240.13e-3, the SEC recognized the potential for overreaching in going private transactions:

> The nature of and methods utilized in effecting going private transactions present an opportunity for overreaching of unaffiliated security holders by an insurer or its affiliates. This is due, in part, to the lack of arms-length bargaining and the inability of unaffiliated security holders to influence corporate decisions to enter into such transactions. Additionally, such transactions have a coercive effect in that security holders confronted by a going private transaction are faced with the prospects of an illiquid market, termination of the protections under the federal securities laws and further efforts by the proponent to eliminate their equity interest.

Exchange Act Release No. 34-17719, *reprinted in* 3 Fed. Sec.L.Rep. (CCH) ¶ 23,709, at 17,245-28 (April 13, 1981).

This Court has also recognized the special problems posed by going private transactions and the need for greater disclosure. In *Radol v. Thomas*, 772 F.2d 244, 255 (6th Cir.1985), *cert. denied*, —— U.S. ——, 106 S. Ct. 3272, 91 L. Ed. 2d 562 (1986), the Court stated:

> The more extensive legal disclosure requirements which apply to freeze-out merger proxy statements are therefore justified by the fact that the law has given the majority the power to foreclose the ownership rights of the minority and has thereby elimi-

> nated the market as a correcting mechanism, leaving minority shareholders with only the option of dissent and appraisal, an option which cannot rationally be exercised unless the majority is compelled to make full disclosure regarding appraisals, earnings, projections and other information that sheds light on the value of the firm.

Rule 13e-3 serves as the primary and most direct vehicle under the federal securities laws for mandating this disclosure in going private transactions. Subsection (e) of Rule 13e-3 prescribes which information from the issuer's Schedule 13e-3 filing with the Commission shall be provided to shareholders as well as the form and content of this public disclosure. *See* 17 C.F.R. § 240.13e-3 (e). Subsection (e) mandates, for example, that where a going private transaction requires the use of a proxy statement, the Rule 13e-3 disclosure be presented in a "Special Factors" section of the proxy statement. 17 C.F.R. § 240.13e-3(e)(1), (3)(i).

Rule 13e-3 does not require that the issuer's Schedule 13e-3 filing with the Commission be reproduced in its entirety in the communication with shareholders. Most items from that Schedule may be summarized. However, Items 7, 8 and 9 must be disclosed verbatim. The rationale behind complete disclosure of these items is that they go to the essence of the transaction. Item 7 requires full disclosure of the purposes, alternatives, reasons, and effects of the transaction; Item 8 requires a statement as to the fairness of the transaction and the factors upon which such belief is based; and Item 9 requires disclosure of reports, opinions, appraisals and certain negotiations.

A. *Item 7 Disclosure*

Item 7 of Schedule 13e-3 requires that the issuer (1) state the purpose for the transaction, (2) discuss any alternative means considered, (3) state the reasons for the structure of the transaction and for its timing, and (4) describe the effects of the transaction on the issuer, its affiliates and unaffiliated security holders. Instruction

2 to Item 7 contains the following guidance: "The description required by Item 7(d) should include a reasonably detailed discussion of the benefits and *detriments* of the Rule 13e-3 transaction to the issuer, its affiliates and unaffiliated security holders. The benefits and detriments of the Rule 13e-3 transaction should be quantified to the extent practicable." (emphasis added).

In the proxy statement, defendants enumerated four reasons for undertaking the transaction: first, eliminating potential conflict of interest problems; second, increasing management flexibility in the insurance and financial markets; third, simplifying the management structure of the Nationwide companies as a whole; and fourth, eliminating the substantial costs of servicing its public shareholders. The proxy statement indicates that the Company considered the possibility of a further tender offer, but rejected this option since the Company did not believe it compared favorably with the going private route in achieving the Company's overall objectives. The proxy statement indicates further that the Company proposed the transaction when it did in order to "maintain their competitive position in the industry." The proxy statement also states that the "[i]nitial out-of-pocket savings to Nationwide Corporation are estimated to be $300,000 per year."

The gravamen of plaintiffs' case on Item 7 compliance appears to be that the proxy statement failed to disclose adequately the "detriment" to Nationwide Mutual of the transaction and thereby concealed the true purpose of the transaction. Plaintiffs argue that a "company does not sacrifice $3,000,000 of annual income in order to save $300,000 and to achieve other nonquantifiable benefits. Having determined that the stated benefits were not genuine, a shareholder would search for the true purpose of the transaction: to acquire the minority interest at a bargain price." Brief of Appellants at p. 37.

In reviewing defendants' Item 7 disclosure, we find as did the District Court that defendants have complied with

this part of Rule 13e-3. Plaintiffs do not suggest specific reasons not enumerated by defendants for undertaking the transaction; their challenge on this point reduces to an attack on the substantive fairness of the transaction. Defendants have specified legitimate reasons for the transaction, and since plaintiffs bear the burden of proof on this issue, plaintiffs' Item 7 challenge must fail.

B. *Item 8 Disclosure*

The instructions accompanying Schedule 13e-3 are quite definite in the level of specificity required in certain disclosures.[5] The Instruction to Item 8 states that "[c]onclusory statements, such as 'The Rule 13e-3 transaction is fair to unaffiliated security holders in relation to net book value, going concern value and future prospects of the issuer' *will not be considered sufficient disclosure in response to Item 8(a).*" (emphasis added.)

The Commission has expressed special concern with disclosures under Item 8(b) of Schedule 13e-3, the Item

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[5] The Instructions to Items 8(b) of the Schedule identify the following factors to be discussed in the disclosure:

> Instructions. (1) The factors which are important in determining the fairness of a transaction to unaffiliated security holders and the weight, if any, which should be given to them in a particular context will vary. Normally such factors will include, among others, those referred to in paragraphs (c), (d) and (e) of this Item and whether the consideration offered to unaffiliated security holders constitutes fair value in relation to:
>
> (i) Current market prices,
>
> (ii) Historical market prices,
>
> (iii) Net book value,
>
> (iv) Going concern value,
>
> (v) Liquidation value,
>
> (vi) The purchase price paid in previous purchases disclosed in Item 1(f) of Schedules 13e-3,
>
> (vii) Any report, opinion, or appraisal described in Item 9 and
>
> (vii) Firm offers of which the issuer or affiliate is aware made by any unaffiliated person, other than the person filing this statement, during the preceding eighteen months . . .

concerning the factors underlying a belief as to the fairness of the transaction. The Commission has issued the following guidance to prospective issuers:

> The Division is concerned that in many instances the Item 8(b) disclosure being made to security holders is vague and non-specific and is therefore of limited utility to security holders. . . . Each such factor which is material to the transaction should be discussed and, in particular, if any of the sources of value indicate a value higher than the value of the consideration offered to unaffiliated security holders, the discussion should specifically address such difference and should include a statement of the bases for the belief as to fairness in light of the difference.

Exchange Act Release No. 34-17719, at 17, 245-42.

The most serious problem in defendants' proxy statement concerns Item 8(b) compliance. Our review of the proxy statement indicates that defendants have made precisely the kind of conclusory statements prohibited by the Rule. In describing the fairness of the transaction as required by Item 8(b), defendants have done nothing more than provide a laundry list of factors considered by their investment banker.[6]

This kind of non-specific disclosure runs counter not only to the SEC's position taken in the Commission release discussed above but also the Instruction to Item 8(b) of Schedule 13e-3. The Instruction states that the issuer shall "[d]iscuss in reasonable detail the material factors upon which the belief stated in Item 8(a) is based and, to the extent practicable, *the weight assigned to each factor.*" (emphasis added). Thus, the proxy statement is incomplete in that we are not provided with any indication of the weights given the various factors as required by Rule 13e-3, incorporating Schedule 13e-3. Moreover, we therefore have no indication as to whether any of the "sources of value indicate a value higher than

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[6] See Appendix A for the relevant language from the proxy statement.

the value of the consideration offended to unaffiliated security holders." Exchange Act Release No. 34-17719, at 17, 245-42.

Instead of providing this itemized disclosure called for by Rule 13e-3, defendants rely heavily on the First Bostion opinion letter to discharge their disclosure obligations.[7] Indeed, the proxy materials state specifically, "Although the Evaluation Committee did not give specific weight to each of the various factors considered in evaluating the fairness of the proposed merger, particular emphasis was placed upon the receipt of the opinion of First Boston."

While the Commission has stated that an issuer in a going private transaction can rely on an investment banker's opinion to meet its disclosure obligations, such opinion itself must fully analyze the factors enumerated in Item 8(b) as well as be "expressly adopted" by the issuer. Exchange Act Release No. 34-17719, at 17, 245-42. The issuer in this case did not conduct its own investigation but chose to rely on the expertise of First Boston. The problem with defendants adopting the First Boston opinion letter as their disclosure to shareholders is that this one-page letter is itself woefully inadequate when measured against the specific disclosure requirements of the Rule. An issuer cannot insulate itself from 13e-3 liability by relying on an investment banker's opinion letter which itself does not comply with the specific disclosure requirements of the Rule. Therefore, defendants' conclusory statements are not cured by conclusory statements made by First Boston in its opinion letter.

Somewhere in the proxy materials the Nationwide shareholders should have received a reasonably detailed analysis of the various financial valuation methods discussed by the Rule and the weights attached thereto.

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[7] See Appendix B for the language from the First Boston opinion letter which appears in the proxy statement as Exhibit II.

Even if certain valuation methods were not particularly relevant, this should itself have been noted and explained. *See* Exchange Act Release No. 34-17719, at 17,245-42. Without this disclosure, Nationwide shareholders did not possess the information necessary to make an informed decision concerning the going private transaction.

C. *Item 9 Disclosure*

Item 9 requires disclosure of various factors relating to appraisals by an outside party. For example, the issuer must disclosure the identity of the outside party; the qualification of the outside party; the method of selection of the outside party; the relationship between the outside party and the issuer over the past two years or any relationship which is contemplated, and any compensation received or to be received; whether the issuer or outside party recommended the amount of consideration to be paid; and a summary of the appraisal.

In the section of the proxy statement entitled "Opinion of the First Boston Corporation," defendants appear to have covered all the elements required in Item 9 disclosure. The proxy statement, for example, reveals the following: First Boston had served as a financial advisor to the Nationwide companies on several matters in the recent past; First Boston recommended the cash-out price of $42.50; and Nationwide Mutual agreed to pay First Boston a fee of $175,000 in connection with the proposed merger as well as all reasonable out-of-pocket expenses, including counsel's fees. The proxy statement also reviewed the information reviewed and relied upon by First Boston.

Plaintiff's main argument on Item 9 compliance centers on one factor considered by First Boston and cited in defendants' proxy statement—"present value of projected future cash flows of the Corporation." Plaintiffs contend that "[s]ince the actual projection of increased revenue and earnings was the most important single

basis for First Boston's recommendation, disclosure was required."

Plaintiff reads more into Item 9 than is actually required: the challenge to Item 9 compliance seems to constitute an Item 8 claim if anything. As the above discussion indicates, Item 9 requires the disclosure of procedural matters. Accordingly, since defendants appear to have complied with this Item, we find no problem in Item 9 compliance.

D. *Rule 13e-3 Liability*

The basic problem with the disposition below is that the District Court did not engage in the detailed analysis required by Rule 13e-3, particularly with respect to Item 8(b) of Schedule 13e-3. The District Court's error in this regard may stem from its reliance on the following language from this Court's decision in *Starkman v. Marathon*, 772 F.2d 231, 240 (6th Cir. 1985): "[w]e have rejected the position that SEC rules regarding freezeout mergers and proxies should determine the disclosure obligations of target management in the first stage of a two-tier tender offer." *Starkman* is inapposite to the present case because this is not the first stage of a two-tier tender offer, but rather the second and final step in this process.

Subsection (b)(2) of Rule 13e-3 states that "it shall be unlawful for an issuer . . . to engage, directly or indirectly, in a Rule 13e-3 transaction unless [the] issuer" . . . complies with the filing, disclosure, and dissemination requirements of the Rule. As discussed above, defendants did not comply with the disclosure obligation imposed by the Rule—a failure declared unlawful by subsection (b)(2) of the Rule. Accordingly, since plaintiffs have a private right of action under § 13(e) to police such unlawful behavior, the District Court erred in its disposition of plaintiffs' Rule 13e-3 claims.

The Antifraud Claims

In addition to liability under subsection (b)(2) of Rule 13e-3, plaintiffs also contend that the defendants breached the antifraud provisions of Rules 10b-5,[8] 13e-3(b)(1),[9] and 14a-9.[10] In essence, plaintiffs contend that

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[8] Securities Exchange Act Rule 10b-5, 17 C.F.R. § 240.10b-5, reads as follows:

> It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interestate commerce, or of the mails or of any facility of any national securities exchange,
>
> (a) To employ any device, scheme, or artifice to defraud.
>
> (b) To make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading, or
>
> (c) To engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person,
>
> in connection with the purchase or sale of any security.

[9] Securities Exchange Act Rule 13e-3(b)(1), 17 C.F.R. § 240.13e-3(b)(1), is virtually identical to Rule 10b-5 and reads as follows:

> It shall be a fraudulent, deceptive or manipulative act or practice, in connection with a Rule 13e-3 transaction, for an issuer which has a class of equity securities registered pursuant to section 12 of the Act or which is a closed-end investment company registered under the Investment Company Act of 1940, or an affiliate of such issuer, directly or indirectly
>
> (i) To employ any device, scheme or artifice to defraud any person;
>
> (ii) To make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in light of the circumstances under which they were made, not misleading; or
>
> (iii) To engage in any act, practice or course of business which operates or would operate as a fraud or deceit upon any person.

[10] Securities Exchange Act Rule 14a-9, 17 C.F.R. § 240.14a-9, reads as follows:

> No solicitation subject to this regulation shall be made by means of any proxy statement, form of proxy, notice of meeting or other communication, written or oral, containing any state-

a failure to disclose information required by Rule 13e-3 *ipso facto* constitutes an "omission" actionable under the antifraud provisions. They argue that Rules 10b-5 and 14a-9 incorporate Rule 13e-3 by reference in the going private context.

The three antifraud provisions at issue here spring from distinct statutes which have unique texts and histories. All three, however, parallel the common law of fraud and deceit. Absent special circumstances, an action for deceit would lie at common law for both falsehoods and half-truths, but not for a complete failure to disclose. *See* III L. Loss, *Securities Regulation* at 1433-35. As was noted by this circuit almost fifty years ago with regard to a similarly worded antifraud provision in the Securities Act of 1933:

> The statute did not require appellant to state every fact about stock offered that a prospective purchaser might like to know or that might, if known, tend to influence his decision, but it did require appellant not "to obtain money or property by means of any untrue statement of a material fact *or any omission to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading.*

Otis & Co. v. SEC, 106 F.2d 579, 582 (6th Cir. 1939) (emphasis in original) (construing § 17(a)(2) of the Securities Act of 1933).

The second clauses of Rules 10b-5 and 13e-3(b)(1), and similar language in Rule 14a-9, adopt the common

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ment which, at the time and in light of the circumstances under which it is made, is false or misleading with respect to any material fact, or which omits to state any material fact necessary in order to make the statements therein not false or misleading or necessary to correct any statement in any earlier communication with respect to the solicitation of a proxy for the same meeting or subject matter which has become false or misleading.

law rule and prohibit silence only where the omitted information is necessary to prevent inaccuracy in existing disclosure. As a result, these provisions have been considered by commentators and the courts alike to be concerned with half-truth rather than omissions *per se*. *See Myzel v. Fields*, 386 F.2d 718, 733 n.6 (8th Cir. 1967); *Trussell v. United Underwriters, Ltd.*, 228 F. Supp. 757, 767 (D. Col. 1964); *Cochran v. Channing Corp.*, 211 F. Supp. 239, 243 (S.D.N.Y. 1962); *see also* III L. Loss, *Securities Regulation* at 1439; A. Bromberg & L. Lowenfels, *Securities Fraud & Commodities Fraud* § 2.6(2).

The essence of plaintiffs' claim is that a failure to provide items of disclosure required by Rule 13e-3(e) always constitutes a material omission under the antifraud rules. This is tantamount to incorporating the disclosure provisions of the securities laws into the antifraud provisions. No longer would omissions be actionable only where a half-truth resulted. Instead, any failure to comply with SEC disclosure obligations would be actionable by private litigants under the antifraud provisions.

Although the antifraud rules are the "catch-all" provisions of the securities laws, the Supreme Court has emphasized in the Rule 10b-5 context that they apply only where some fraud has been committed. *See Chiarella v. United States*, 445 U.S. 222, 234-35, 100 S. Ct. 1108, 1117-18, 63 L. Ed. 2d 348 (1980). Congress did not enact sections 10(b), 13(e), or 14(a) to give private litigants the same enforcement powers granted to the Commissioner of the SEC. Allowing private suits based ony any non-disclosure, without regard to the "half-truth" limitation, would contravene the congressional intent behind these statutes. Therefore, we hold that omission of disclosure required by Rule 13e-3(e) will constitute a violation of the antifraud provisions of sections 10(b), 13(e), and 14(a) only where the information is necessary to prevent half-truth. The violations of Rule 13e-3, Item

8, itemized above, do not constitute "fraud" under sections 10(b) and 14(a) but should be considered as volations only of the specific rule in question.[11]

REMAND ORDER

The case is remanded to the District Court with instructions to reconsider defendants' failure to provide Item 8 information in the violation of Rule 13e-3, as established by this opinion. The District Court should also consider issues of materiality of the defendants' mission under Rule 13e-3. After reconsidering the federal claims under Rule 13e-3, the District Court should determine whether it is necessary to decide the alternative state claims respecting breach of fiduciary duty. If so, the District Court's disposition of the state claims should be accompanied by detailed findings of fact and conclusions of law concerning the state standard of fiduciary duty used by the Court.

Accordingly, the judgment of the District Court is reversed and remanded for proceedings consistent with this opinion.

GUY, Circuit Judge, concurring in part and dissenting in part.

Although I concur in most of Judge Merritt's well-written and thorough opinion, I disagree with the conclusions reached in Part B, Item 8, Disclosure. Since it is this part of the court's decision that results in this case being remanded, I must dissent.

I believe the district court properly analyzed plaintiffs' disclosure claims pursuant to Rule 13e-3, which sets forth disclosure requirements for going-private mergers, notwithstanding that the disclosure requirements under

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[11] Under certain circumstances, violations of Rule 13e-3 may be indicative of a "scheme or artifice to defraud" which would violate the antifraud provisions. Such is not the case here, however, where non-disclosure is claimed to be a violation standing alone.

Rule 13e-3 are more detailed in a going-private transaction than in other types of mergers. *See Radol v. Thomas*, 772 F.2d 244, 254-55 (6th Cir. 1985), *cert. denied*, —— U.S. ——, 106 S. Ct. 3272, 91 L. Ed. 2d 562 (1986) (as quoted in the majority opinion). Along with Rule 13e-3, the regulations provide an itemized list of information which must be included in the proxy statement. In accord with this list, plaintiffs' claims relating to alleged inadequate disclosure can be separated into three components. First, plaintiffs claim that the proxy statement did not adequately disclose the "benefits and detriments" of the merger. Second, plaintiffs claim that the proxy statement did not sufficiently explain why the merger occurred at the time that it did. Finally, plaintiffs contend that the proxy statement did not discuss the fairness of the transaction in sufficient detail. As I read the majority opinion, it is only that part of the district court's decision dealing with the fairness of the transaction with which they find fault.

Item 8 of Schedule 13e-3, 17 C.F.R. § 240.13e-100, requires:

> Item 8. *Fairness of the Transaction.* (a) State whether the issue or affiliate filing this schedule reasonably believes that the Rule 13e-3 transaction is fair or unfair to unaffiliated security holders.
>
> . . . .
>
> (b) Discuss in reasonable detail the material factors upon which the belief stated in Item 8(a) is based and, to the extent practicable, the weight assigned to each such factor. Such discussion should include an analysis of the extent, if any, to which such belief is based on the factors set forth in instruction (1) to paragraph (b) of this Item, paragraphs (c), (d), and (e) of this Item, and Item 9.
>
> *Instructions.* (1) The factors, which are important in determining the fairness of a transaction to

unaffiliated security holders and the weight, if any, which should be given to them in a particular context will vary. Normally such factors will include, among others, those referred to in paragraphs (c), (d), and (e) of this Item and whether the consideration offered to unaffiliated security holders constitutes fair value in relation to:

(i) Current market prices,

(ii) Historical market prices,

(iii) Net book value,

(iv) Going concern value,

(v) Liquidation value,

(vi) The purchase price paid in previous purchases disclosed in Item 1(f) of Schedule 13e-3,

(vii) Any report, opinion, or appraisal described in Item 9 and

. . . .

(c) State whether the transaction is structured so that approval of at least a majority of unaffiliated security holders is required.

(d) State whether a majority of directors who are not employees of the issuer has retained an unaffiliated representative to act solely on behalf of unaffiliated security holders for the purposes of negotiating the terms of a Rule 13e-3 transaction and/or preparing a report concerning the fairness of such transaction.

(e) State whether the Rule 13e-3 transaction was approved by a majority of the directors of the issuer who are not employees of the issuer.

Plaintiffs contend that in setting forth the factors upon which the fairness determination was made, the proxy statement did not adequately discuss the "going concern value," the "net asset value," or the "liquidation value"

of Nationwide. Plaintiffs' argument is not persuasive for a number of reasons. First, plaintiffs are incorrect in asserting that Nationwide was *required* to discuss these factors in the proxy statement. Item 8 does not require the discussion of any factor, it only sets forth the factors which "normally" will be included. Moreover, the detail of the discussion of any single factor will necessarily depend upon the weight, if any, which was placed upon the factor in reaching a fairness decision. Second, each of the factors which plaintiffs contend were not adequately discussed were at least mentioned in the fairness discussion. The statement explains that First Boston, which independently considered the fairness of the price, considered these factors in reaching its conclusion. Third, and most importantly, the fairness discussion sets forth clearly and in reasonable detail the factors upon which defendants relied in reaching their fairness conclusion.

The proxy statement explained:

> Although the Evaluation Committee did not give specific weight to each of the various factors considered in evaluating the fairness of the proposed merger, particular emphasis was placed upon the receipt of the opinion of First Boston.
>
> The members of the Evaluation Committee believed it to be particularly important that the price to be paid to the public shareholders for their Class A Common shares ($42.50 per share) represented a premium over the quoted bid price of the Class A Common shares on the next to last trading day prior to the public announcement of the proposed merger on November 3, 1982, as reported by the National Quotation Bureau, Inc.
>
> In evaluating the overall fairness of the proposed merger, the Evaluation Committee also considered it significant that First Boston would notify the Corporation on the date hereof and on the date

immediately preceding the effective date of the merger if events render the financial terms of the proposed merger unfair to the public shareholders; that the Corporation's Class A Directors (five out of six of whom constitute the Evaluation Committee) would have the authority under the Agreement to terminate the Agreement if a majority of public shareholders fail to approve the proposed merger; that the terms of the Agreement were negotiated by independent legal counsel retained by the Evaluation Committee; that the Agreement may be terminated in the event the Corporation receives, prior to the special meeting of the shareholders, a bona fide offer to acquire the publicly held Class A Common shares which offer, in the judgment of the Class A Directors, is more favorable to the public shareholders than the proposed merger; and that the Evaluation Committee had been given full authority to evaluate, make recommendations regarding and respond to offers made or proposed to be made to the Corporation by Nationwide Mutual or any of its affiliates. The Evaluation Committee consisted solely of Class A Directors of the Corporation who are neither directors, officers nor employees of Nationwide Mutual or Nationwide Mutual Fire, nor officers or employees of the Corporation.

Considered in its entirety, I would conclude that the fairness discussion contained in the proxy statement satisfies the disclosure requirements set forth in Item 8. In this regard, it is important to emphasize that the issue before us is not whether the price arrived at was fair, but rather, whether the proxy statement adequately discussed the factors upon which Nationwide could reasonably conclude that the price was fair to the unaffiliated shareholders. The methodology employed in this merger to arrive at a price, including an independent appraisal as well as a review by the Evaluation Committee, supplied

a reasonable basis for believing that the ultimate price arrived at was fair.

Plaintiffs also argue that the fairness discussion should have disclosed data about other companies involved in "comparative transaction." Neither Rule 13e-3, nor Schedule 13E-3 contain any requirement that a going-private proxy statement provide any comparative data on mergers involving other companies. Moreover, plaintiffs cite no cases to support this argument. Since there is no evidence indicating that Nationwide relied upon such data in reaching its conclusion regarding the fairness of this transaction, disclosure was not required. In addition, because such information has the potential to mislead, other courts have held that such information is not material and need not be included in a proxy statement. *Mindell v. Greenberg*, 612 F. Supp. 1543, 1551 (S.D.N.Y. 1985) ("The fact that other transactions might have been negotiated on terms plaintiff may have found more favorable is irrelevant"); *Gans v. Filmways, Inc.*, 453 F. Supp. 1116, 1120 (E.D. Pa. 1978), *aff'd*, 595 F.2d 1212 (3d Cir. 1979) ("insurance companies are not fungible entities and the value of one company is not a reliable indication of the value of another").

Plaintiffs also contend that the fairness discussion should have disclosed the "fact" that Nationwide's public stock was "thinly traded." This fact according to plaintiffs would tend to offset the importance of the fact that the price offered by Mutual represented a premium of 51.8% over the stock's market price. This argument conflicts with the well-established rule that the proxy statement must set forth a full and fair picture, without interpretation or characterization. *Santa Fe Industries, Inc. v. Green*, 430 U.S. 462, 474-77, 97 S. Ct. 1292, 1301-1303, 51 L. Ed. 2d 480 (1977). As disclosed in the proxy statement, Nationwide's Class A Common stock was traded in the over-the-counter market, and 85.6% of the shares were owned by Mutual. Whether under these circumstances the stock should be characterized as "thinly

traded," is difficult to say—which is the reason why this type of conclusion need not be included in a proxy statement. The facts speak for themselves.

I would affirm the district court.

APPENDIX A [To Sixth Circuit Opinion]

The proxy statement provides in pertinent part:

> The members of the Evaluation Committee believe that, from a financial point of view, the terms of the proposed merger are fair to the public shareholders of the Corporation. The committee members considered important, as an indication of the fairness of the proposed merger, the receipt of the written opinion of First Boston. The committee members also considered important a number of other factors discussed with the representatives of First Boston. These factors are the current market price of the Class A Common shares as compared with stock prices of other comparable entities; past and current earnings of the Corporation; past and current price/earnings ratios of the Corporation and other companies having similar operations; past and current price/equity ratios of the Corporation (as computed in accordance with generally accepted accounting principles); and the premium over market price offered to the public shareholders in other similar transactions as well as in other recent acquisitions in the life insurance industry generally. In its discussions with the representatives of First Boston, upon whose opinion the Evaluation Committee has concluded that it is appropriate to rely, these representatives stated that in addition to the above noted factors they had also considered the current overall level of the stock market; historical market prices of the Class A Common shares as compared with market prices for the stock of other comparable entities; going concern value of the Corporation; net book value of the Corporation; liquidation value of the Corporation; various financial ratios; present revenues, expenses, earnings and dividends of the Corporation and trends with respect thereto; the purchase price paid to holders of Class A Common

shares by Nationwide Mutual in connection with the December 1978 tender offer for the Class A Common shares; present value of projected future cash flows of the Corporation; replacement value of the Corporation; off balance sheet items of the Corporation; significant trends in the insurance business; competitive environment of the insurance industry; regulatory environment of the insurance industry; and the impact of inflation on the Corporation.

Joint Appendix pp. 545-46.

APPENDIX B [To Sixth Circuit Opinion]

The First Boston opinion letter reads in its entirety as follows:

November 1, 1982

Board of Directors
Nationwide Corporation
One Nationwide Plaza
Columbus, Ohio 43216

Gentlemen:

You have asked us to advise you as to the fairness to the shareholders of Nationwide Corporation, other than Nationwide Mutual Insurance Company and Nationwide Mutual Fire Insurance Company, of the financial terms of a proposed merger whereby the owners of 685,545 publicly held Class A common shares would receive cash for their shares and Nationwide Mutual Insurance Company and Nationwide Mutual Fire Insurance Company would become the only shareholder of Nationwide Corporation. The terms of the merger transaction are that Nationwide Corporation shareholders will be entitled to receive $42.50 for each share of Nationwide Corporation Class A common shares.

In connection with our review, Nationwide Corporation furnished to us certain business and financial data concerning Nationwide Corporation. This information was furnished specifically for the purpose of our advising you as to the fairness of the financial terms of the proposed merger, and our Corporation's representation that the information is complete and accurate in all material respects. We have not independently verified the information. We have also reviewed certain publicly available information that we considered relevant and have had discussions with certain members of Nationwide Corporation's management.

In arriving at our opinion we have also considered, among other matters we deemed relevant, the historical

financial record, operating statistics, current financial position and general prospects of Nationwide Corporation and the stock market performance of the Class A common shares of Nationwide Corporation. In addition, we have considered the terms and conditions of the proposed transaction as compared with the terms and conditions of comparable transactions.

Based on our analysis of the foregoing and of such other factors as we have considered necessary for the purpose of this opinion and in reliance upon the accuracy and completeness of the information furnished to us by Nationwide Corporation, it is our opinion that the financial terms of the proposed transaction are fair to the minority shareholders of Nationwide Corporation.

Very truly yours,

THE FIRST BOSTON
CORPORATION

Joint Appendix p. 600.

UNITED STATES DISTRICT COURT
S.D. OHIO, W.D.

Nos. C-1-83-1693, C-2-82-1385

HOWING COMPANY, *et al.*,
Plaintiffs,

v.

NATIONWIDE CORPORATION, *et al.*,
Defendants.

BELLE EFROS,
Plaintiff,

v.

NATIONWIDE CORPORATION, *et al.*,
Defendants.

Oct. 18, 1985

William R. Jacobs, Douglas G. Cole, Cincinnati, Ohio, for plaintiffs Howing Co., et al.

Kenneth R. Cookson, Columbus, Ohio, Gene Mesh, Cincinnati, Ohio, for plaintiff Efros.

Frederick J. McGavran, Cincinnati, Ohio, Jeffrey Davidson, Daniel Attridge, John Whatley, Kirkland & Ellis, Washington, D.C., for defendants.

OPINION AND ORDER

SPIEGEL, District Judge.

PROCEEDINGS

This matter came on for consideration and decision on the oral arguments of the parties on defendants' motion for summary judgment (doc. 95), with exhibits attached,

defendants' corrected memorandum in support (doc. 96), plaintiffs' cross-motion for partial summary judgment (doc. 99), and memorandum in opposition to defendants' motion for summary judgment (doc. 100), with exhibits, defendants' reply memorandum in support of their motion for summary judgment (doc. 103), plaintiffs' supplemental memorandum in support of their motion for partial summary judgment and *contra* defendants' motion for summary judgment (doc. 105), which we granted leave to plaintiffs to file at the oral arguments held on September 30, 1985, defendants' supplemental memorandum in support of their motion for summary judgment (doc. 106), and supplemental memorandum of plaintiffs regarding issues of exclusivity of appraisal proceedings (doc. 107).

FACTUAL BACKGROUND

In this litigation, plaintiffs challenge the 1983 merger between Nationwide Corporation (Nationwide Corp.) and First Plaza Corporation (First Plaza), in which Nationwide Corp. became solely owned by Nationwide Mutual Insurance Corp. (Nationwide Mutual) and its affiliate Nationwide Mutual Fire Insurance Company (Nationwide Fire). The shares of Class A common stock of Nationwide Corp. were converted under the terms of the merger into the right to receive $42.50 per share in cash, or the fair cash value thereof, under Section 1701.85, O.R.C.

The corporate structure of defendants is as follows: Nationwide Mutual was the owner of 85.6% of the outstanding Class A common shares of Nationwide, and Nationwide Mutual and Nationwide Mutual Fire Insurance Company owned 100% of the outstanding Class B common share of Nationwide. The public owned the remaining 14.4% of the outstanding Class A common shares of Nationwide. Nationwide Mutual is the parent of a number of subsidiary corporations, including Nationwide Mutual Fire Insurance Company, Nationwide Life Insurance

Company, Michigan Life Insurance Company, West Coast Life Insurance Company, Gulf Atlantic Life Insurance Company, and National Casualty Company.

Nationwide Mutual is engaged in the business of holding substantial or controlling stock interests, primarily in life insurance and financial service corporations.

Nationwide's proxy statement of December 9, 1982 accurately recounts the history of the proposed merger:

> In September, 1982, certain officers of Nationwide Mutual informally approached the President of the Corporation proposing the transaction. They discussed the general terms of the possibility of an acquisition by Nationwide Mutual of the remaining publicly held Class A common shares of the corporation for cash. They also proposed affecting a similar acquisition with respect to the outstanding publicly held shares of stock of Nationwide Life, the principal operating subsidiary of the Corporation. . . . In each transaction, Nationwide Mutual proposed that the public shareholders would receive cash for their shares. The president subsequently contacted the two other members of the executive committee of the Board of Directors of the Corporation who were not directors, officers, or employees of Nationwide Mutual or Nationwide Mutual Fire. The President reported on his discussions concerning the proposal. Following their preliminary discussions, those unaffiliated members of the corporation's Executive Committee retained independent legal counsel to advise them in respect of the proposal and to represent the interest of the public shareholders of the Corporation.
>
> At a special meeting of the directors held on November 2, 1982, the directors of the Corporation were advised that on the following day the Investment Committee of Nationwide Mutual's Board of Direc-

tors would recommend to its full Board, and Nationwide Mutual's Board of Directors would consider, a proposal which, if made and accepted, would provide for the merger of the corporation and First Plaza, newly created, wholly owned subsidiary of Nationwide Mutual. As part of the proposal, the corporation would become a wholly owned subsidiary of Nationwide Mutual and Nationwide Mutual Fire, and the corporation's public shareholders would receive $42.50 per share in cash for the Class A common shares. The Corporation's directors were advised that the price to be paid to the public shareholders for their shares had been set by Nationwide Mutual's Investment Committee to reflect a fair value thereof as determined by the First Boston Corporation ("First Boston").

Immediately thereafter, the Board of Directors of the Corporation appointed a special Evaluation Committee, consisting of the corporation's five Class A Directors who are neither directors, officers, nor employees of Nationwide Mutual or Nationwide Mutual Fire, nor employees of the Corporation, to consider the proposal and to make a recommendation in respect thereof to the full board. The Evaluation Committee was given full authority to hire any professional advisers which it deemed necessary to fulfill its responsibility.

The Evaluation Committee then met that morning to consider engagement of independent counsel to represent the interests of the public shareholders and to advise the Evaluation Committee in respect to the proposed merger. The Evaluation Committee determined to retain the special counsel previously engaged to advise the unaffiliated members of the Executive Committee in respect of the proposal, and immediately thereafter met with such independent counsel to consider the proposal. Counsel advised the

members of the Evaluation Committee of their fiduciary responsibilities to the public shareholders, and recommended that the Evaluation Committee meet with representatives of First Boston to consider the adequacy of the price from a financial point of view. Counsel also advised the Evaluation Committee of the need to consider, and the Evaluation Committee considered the statements of officers of both the corporation of Nationwide Mutual in respect of the existence of a proper business purpose for such a transaction.

On the afternoon of November 2, 1982, the Evaluation Committee met with representatives of First Boston, who at that time reported to the members of the Evaluation Committee that in First Boston's opinion, the proposed price of $42.50 per share was fair to the public shareholders of the corporation from a financial point of view. . . . After further consultation with counsel in respect of the proposal, and after reviewing in detail the report of First Boston in respect of the fairness of the proposed price, and discussing with representatives thereof the terms of its engagements and the scope of its opinion, the Evaluation Committee determined to recommend to the full Board of Directors of the Corporation that the Corporation accept Nationwide Mutual's proposals made on the terms presented to the Evaluation Committee.

On the following day, November 3, 1982, the Board of Directors of the Corporation met in joint session with the Boards of Directors of Nationwide Mutual and Nationwide Mutual Fire, and Nationwide Mutual formally presented the proposal to the Corporation. . . . The joint session was addressed by representatives of First Boston in respect of the proposed price payable to the public shareholders of the Corporation for their Class A Common shares . . . . Upon

> review of the report of the First Boston at the joint session, and based upon the recommendation of the Evaluation Committee in respect of the proposal, the Board of Directors of the corporation unanimously voted to enter into an agreement merger with First Plaza, a wholly-owned subsidiary of Nationwide Mutual, whereby the corporation would become solely owned by Nationwide Mutual and Nationwide Mutual Fire, and the public shareholders of the Corporation would receive $42.50 in cash for their Class A Common shares. Pursuant thereto, the Corporation, Nationwide Mutual, and First Plaza entered into the agreement of merger.

(doc. 95, Exhibit A, pp. 9 and 10). When the proposed merger was publicly announced on November 3, 1982, the closing bid price of the previous day for the Class A common shares was $28 per share. The merger price of $42.50 represented a premium of 51.8% over the market price, and the merger price was equal to 106% of the June 30, 1982 per share book value of $40.20 and 12.1 times the previous 12 months per share earnings at $3.51.

The proxy materials were distributed to approximately 4,000 public stockholders on December 9, 1982, describing the history and purpose of the proposed transaction, and the action taken by the First Boston and the Evaluation Committee, and contained extensive Nationwide financial information. The materials notified the stockholders of the special meeting to be held January 18, 1983 for the purpose of voting on the merger, and also notified the stockholders of the right to seek judicially determined fair cash value under Ohio Revised Code § 1701.85. Mrs. Efros filed her complaint against Nationwide on November 9, 1982 a preliminary injunction which was denied on January 14 (docs. 16 and 17) and Findings of Fact and Conclusions of Law filed on January 17, 1983 (doc. 20 and 21). Following the denial of Mrs. Efros' motion for a preliminary injunction, the merger was approved by

Nationwide public stockholders at the January, 1983 meeting with 94.7% of the voted public shares favoring the merger. None of the named plaintiffs in this litigation participated in the balloting, nor did any shareholder elect to proceed in the Ohio courts to determine the fair cash value pursuant to the remedies available in Section 1701.85 of the Ohio Revised Code.

QUESTIONS PRESENTED

The complaints filed by Mrs. Efros, the Howing Company, and Douglas McClellan, allege that Nationwide has violated the Federal Securities Law by making false and misleading statements in its announcement of the proposed merger. The defendants have vigorously denied them.

The pleadings, cross-motions for summary judgment, and the oral arguments of the defendants contend that plaintiffs' position does not present a cognizable claim under the Federal Securities Laws. Defendants argue that Nationwide Corp.'s materials contain no material misrepresentation or omissions required under the Federal Securities Laws, that since there has been full disclosure by defendants, plaintiffs' claim that the merger was unfair is not a cognizable claim under the Federal Securities Laws, that the issue of fairness actually relates to the adequacy of the price per share, and that if plaintiffs were dissatisfied with the price, the only available remedy was that provided by Ohio Revised Code Section 1701.85 for judicially determined fair cash value. Finally, defendants contend that there is no evidence of any breach of fiduciary duty owed plaintiffs by defendants, and since, under Ohio corporation law the merger was neither unauthorized by statute, illegal, nor ultra vires, Ohio statutory appraisal rights constituted plaintiffs' exclusive state law remedy.

Plaintiffs, in opposition to defendants' motion for summary judgment contend that there are genuine issues of

material fact relating to the determination and fairness of the merger price, and in support of their motion for partial summary judgment, argue that the proxy statement of Nationwide failed to meet the disclosure requirements imposed by Rule 13e-3, 17 C.F.R. § 240.13e-3. Specifically, they contend that the proxy statement failed to disclose the detriments and benefits resulting from the merger, failed to disclose the reasons for the timing of the transaction, failed to comply with the requirements of Rule 13e-3 that the fairness of the merger be discussed in reasonable detail, failed to address all material factors relating to value, and that there was an inadequate discussion of the market price and the First Boston's opinion.

At oral argument, the parties agreed that there really are no contested issues of fact, and that the disposition of this litigation can be decided on what has been filed with the Court in support of the cross-motions for summary judgment.

DECISION

We begin our analysis by recognizing that Rule 13e-3 promulgated pursuant to Section 13 of the Act establishes the standard of conduct that must be met by an issuer in this type of transaction. What we have here is a freeze-out merger. Rule 13e-3 relates to going private transaction by certain issuers or their affiliates. The disclosure requirements in a freeze-out merger proxy statement are more extensive than those in other types of proxies as noted by Judge Merritt in *Radol v. Thomas*, 772 F.2d 244 (6th Cir. 1985). Judge Merritt notes:

> The more extensive legal disclosure requirements which apply to freeze-out merger proxy statements are therefore justified by the fact that the law has given the majority the power to foreclose the ownership rights of the minority and has thereby eliminated the market as a correcting mechanism, leaving minority shareholders with only the option of dissent and appraisal, an option which cannot rationally

> be exercised unless the majority is compelled to make full disclosure regarding appraisals, earnings projections, and other information that sheds light on the value of the firm.

Id. at pp. 254-55.

We therefore will review the proxy material of Nationwide Corporation to see if it meets the standards of disclosure required by Rule 13e-3. If in any instance there has been a failure to meet the standard, we will then examine whether such failure constitutes a material breach, and if we conclude that there is a jury question concerning the materiality of the breach, then, of course, there would be a genuine issue of fact to be determined. The test for materiality which we will utilize and which the parties agreed is appropriate in this situation is the test applied by the Supreme Court in *TSC Industries, Inc. v. Northway, Inc.*, 426 U.S. 438, 449, 96 S. Ct. 2126, 2132, 48 L. Ed. 2d 757 (1976), whether there is a "substantial likelihood that, under all the circumstances the omitted fact would have assumed actual significance in the deliberations of the reasonable shareholders." Thus, if we conclude that there is no substantial likelihood that the omission would have been significant in the deliberation of a reasonable shareholder, then there would be no question for a jury to decide. Otherwise, it will be left to the trier of fact to decide whether there has been a material misstatement or omission that falls below the standard mandated by Rule 13e-3 and, if so, the jury must then determine the reasonable value of the stock which plaintiffs' class should have been paid at the time the merger was consummated.

At the oral argument and in the briefs, in a further attempt to focus on the issues of this case, the parties agree that the issue of liability was a mater of law for resolution by the Court since there exists no relevant or material conflicts in testimony or other issues appropriate for a jury, and plaintiffs' complaint can be boiled down to

three general contentions. First, that the proxy statement did not sufficiently discuss the detriments and benefits resulting from the merger; second, that the proxy statement did not sufficiently discuss the timing of the merger proposal; and, third, that the proxy statement did not discuss the fairness of the merger in sufficient detail.

I. Our examination begins with a review of the proxy statement and Item 7 of Schedule 13e-3, 17 C.F.R. § 240.13e-100, in order to determine whether the statement sufficiently discusses the detriments and resulting benefits from the merger.

Based upon our review of the proxy statement, we conclude that the requirement of a reasonably detailed discussion of the benefits and detriments was set forth prominently in the forepart of that document. The portion of the proxy statement entitled "Effect of the Transaction" disclosed that upon successful completion of the merger, First Plaza would cease to exist and that Class A Common shareholders would receive $42.50 per share, which was substantially over market value and book value. The proxy statement proceeded to explain the possible tax consequences of the transaction and the fact that the public stockholders' interests would be extinguished.

The parties agree that the proxy statement contains a discussion of the intended benefits to Nationwide Mutual under the portion of the statement entitled "Purposes of the Transaction." However, plaintiffs contend that the information therein is not meaningful as the discussion is "boilerplate" and contains "patently contrived excuses for eliminating the minority interests." We disagree. The statement discloses four distinct purposes for the transaction. First, the elimination of public shareholder interests would alleviate potential conflict of interest problems presented by the presence of minority shareholder interests in respect to transactions involving the

Corporation and its affiliates; second, the proposed merger would increase management flexibility; third, elimination of public shareholder interests would permit management to simplify management structure in order to avoid duplication of efforts; and fourth, the merger would result in the elimination of substantial costs in servicing the public shareholders. The proxy statement further notes that "Nationwide Corporation and Nationwide Mutual have not placed a monetary value on the benefits to be derived from the proposed transaction."

We recognize that the benefits to Nationwide Mutual may be difficult, if not impossible, to accurately quantify and conclude that the benefits to Nationwide Mutual resulting from the elimination of public shareholders were sufficiently set forth. Furthermore, there may be sound business reasons for not making such a quantification. We agree with Judge Rubin, who, after examining these identical four purposes, stated that "any attempt to quantify such expectations [anticipated advantages of the merger] might be met with legitimate charges of misrepresentation." *Efros v. Nationwide Corp.*, [1982-83] Fed. Sec. L. Rep. (CCH) ¶ 99,077 (S.D. Ohio 1983). We are reluctant to say that the purposes for the merger articulated in the proxy statement were contrived. "The business judgment rule recognizes that many important corporate decisions are made under conditions of uncertainty, and it prevents courts from imposing liability on the basis of judicial hindsight. . . ." *Radol v. Thomas*, 772 F.2d at 257. We decline to second guess the directors of Nationwide as to the stated purpose for the merger and decline to quantify the benefits and detriments of the merger ourselves.

Plaintifls further argue that the fact Mutual was financing the transaction from its own funds and that Mutual was sacrificing annual income of three million dollars to achieve the merger was a material fact which should have been disclosed. Plaintiffs' argument is not

well-taken as the proxy statement clearly disclosed that Nationwide Mutual was providing the funds to finance the transaction, and we are not convinced that defendants were required to do more than that. Furthermore, a shareholder could surmise the approximate amount Nationwide Mutual was paying for the total number of Class A shares by reviewing the detailed financial information contained in the proxy statement.

Finally, plaintiffs contend that the proxy statement should have disclosed that as a result of the merger, Mutual would obtain a complete ownership interest in Nationwide and its assets at a proportionate value substantially in excess of the cash-out price. However, as we noted previously, many of the benefits of the transaction are unquantifiable, and it would be an imposition upon the business judgment of the drafters of the proxy statement to require them, in hindsight, to quantify these benefits. Moreover, we find that the financial picture was fully disclosed and therefore a reader of the proxy statement could easily determine that one of the advantages of the merger might be that Mutual would gain additional assets from the transaction.

We conclude that the detriments and benefits were adequately discussed in the proxy statement and that the gravamen of plaintiffs' argument on this issue is actually that the merger price itself was not fair to the public stockholders. However, our concern is not the specific terms of the transaction, but rather, whether there was full disclosure in the proxy statement, *Santa Fe Industries v. Green*, 430 U.S. 462, 477-78, 97 S. Ct. 1292, 1302-03, 51 L. Ed. 2d 480 (1977) and we find that requirement was satisfied.

II. The second part of our analysis concerns whether the proxy statement adequately disclosed the reasons for undertaking the transaction at the particular time in question, as required by Item 7 to Schedule 13E-3. The reason given in the proxy statement was that "the posi-

tion of the Nationwide Companies in the insurance industries requires them to increase flexibility and maximize cost savings to maintain their competitive position in the industry." The plaintiffs dismiss this statement as meaningless because that statement "would be true at any time." Furthermore, they assert that the earnings projections made by First Boston and Nationwide regarding future increases in earnings should have been disclosed in the proxy statement, as that was the true undisclosed purpose for undertaking the transaction at that particular time. Again, plaintiffs ask us to second guess the directorial actions and replace their judgment with our own judgment or opinion as to why the transaction was undertaken. We decline to do so. We conclude that defendants were not required to disclose earnings projections in the proxy statements. Judge Merritt noted in *Radol v. Thomas*, 772 F.2d 244:

> In *Starkman v. Marathon Oil Co.*, 722 F.2d 231 (6th Cir. 1985), we have reaffirmed our adherence to the basic rule established by our prior decisions that tender offer materials must disclose soft information, such as these asset appraisals based upon predictions regarding future economic and corporate events, *only if the predictions underlying the appraisal are substantially certain to hold.*

Id. at 252 (emphasis added).

In *Biechele v. Cedar Point, Inc.*, 747 F.2d 209 (6th Cir. 1984), the Court held that a target's failure to disclose an appraisal based upon cash flow and earnings projections, intended to be used as a selling document in merger negotiations, did not violate Rule 10b-5, as the "selling document" and valuation based upon replacement cost of assets could be misleading to the shareholder. We conclude that the earnings projections made by First Boston and Nationwide was "soft" information,

not substantially certain to hold, and therefore, it was not required to be disclosed under the proxy laws.[1]

III. Finally, we must determine whether the proxy statement complied with the requirements of Item 8 of Schedule 13E-3 that the fairness of the merger be discussed in reasonable detail. Plaintiffs acknowledge that the proxy statement specifically states that the members of the Evaluation Committee believed the transaction was a fair one. However, plaintiffs assert that the belief must be expressed as a reasonable one, which was not the situation here because the "Evaluation Committee and Board of Directors could not possibly have a sufficient basis to form a reasonable opinion." Plaintiffs correctly point out that Schedule 13E-3 requires a discussion, in reasonable detail, of all material factors upon which the reasonable belief as to fairness is based and to the extent practicable, the weight to be assigned to each factor. The rule provides that:

> Such discussion should include an analysis of the extent, if any, to which such belief is based on the factors set forth [below] and Item 9.[2]

17 C.F.R. § 240.13e-100.

The fairness opinion rendered by Nationwide in the proxy statement, in pertinent part, was as follows:

> [T]he directors considered important, (i) the various business purposes addressed by management

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[1] Additional discussion about the disclosure of earnings projections in proxy statements is contained in the portion of our Opinion addressing plaintiffs' contention that the proxy statement did not discuss the First Boston opinions in sufficient detail.

[2] The facts include current and historical market price of the stock, the book, liquidation and going concern values of the corporation; and the price paid in preivous purchases. Item 9 requires the issuer or affiliate to state whether it has received any report, opinion or appraisal from an outside party which is materially related to the Rule 13e-3 transaction.

which the proposed merger will accomplish (see "SPECIAL FACTORS—Purposes of the Transaction"); (ii) the written opinion of First Boston to the effect that the financial terms of the proposed merger were fair to the public shareholders of the Corporation (a copy of which is attached to this Proxy Statement as EXHIBIT II); and (iii) the report of the Evaluation Committee, that it believed the financial terms of the proposed merger to be fair to the public shareholder, based upon both First Boston's opinion and its review with representatives of First Boston of the terms and conditions of First Boston's engagement, and the scope of the investigation in giving the opinion.

The Evaluation Committee carefully reviewed with representatives of First Boston the terms of its engagement in this matter, particularly in respect of its relationship with Nationwide Mutual. The members of the Evaluation Committee concluded that, based upon its discussions with such representatives, it was appropriate in this case to rely upon First Boston's valuation and opinion in determining the fairness of the financial terms of the proposed merger to the public shareholders.

The members of the Evaluation Committee believe that, from a financial point of view, the terms of the proposed merger are fair to the public shareholders of the Corporation. The committee members considered important, as an indication of the fairness of the proposed merger, the receipt of the writtent opinion of First Boston. The committee members also considered important a number of other factors discussed with the representatives of First Boston. These factors are the current market price of the Class A Common shares as compared with stock prices of other comparable entities; past and current earnings of the Corporation; past and current price/earnings ratios of the Corporation and

other companies having similar operations; past and current price/equity ratios of the Corporation (as computed in accordance with generally accepted accounting principles); and the premium over market price offered to the public shareholders in this transaction as compared to recent premiums paid to minority shareholders in other similar transactions as well as in other recent acquisitions in the life insurance industry generally. In its discussion with the representatives of First Boston, upon whose opinion the Evaluation Committee has concluded that it is appropriate to rely, these representatives stated that in addition to the above noted factors they had also considered the current overall level of the stock market; historical market prices of the Class A Common shares as compared with market prices for the stock of other comparable entities; going concern value of the Corporation; net book value of the Corporation; liquidation value of the Corporation; various financial ratios; present revenues, expenses, earnings and dividends of the Corporation and trends with respect thereto; the purchase price paid to holders of Class A Common shares by Nationwide Mutual in connection with the December 1978 tender offer for the Class A Common shares; present value of projected future cash flows of the Corporation; replacement value of the Corporation; off balance sheet items of the Corporation; significant trends in the insurance business; competitive environment of the insurance industry; regulatory environment of the insurance industry; and the impact of inflation on the Corporation.

Although the Evaluation Committee did not give specific weight to each of the various factors considered in evaluating the fairness of the proposed merger, particular emphasis was placed upon the receipt of the opinion of First Boston. The members of the Evaluation Committee believed it to be par-

ticularly important that the prices to be paid to the public shareholders for their Class A Common shares ($42.50 per share) represented a premium over the quoted bid price of the Class A Common shares on the next to last trading day prior to the public announcement of the proposed merger on November 3, 1982, as reported by the National Quotation Bureau, Inc.

The plaintiffs advance three arguments in regard to the fairness opinion. First, that the proxy statement did not sufficiently discuss the net book value, liquidation value, and going concern value of Nationwide; second, that the proxy statement did not explicitly state that the Nationwide stock was "thinly traded"; and third, that the proxy statement did not sufficiently discuss the basis for the First Boston fairness opinion.

As to plaintiff's first contention, we note that the proxy statement contained extensive financial information necessary to compute the net book, liquidation, and going concern values of Nationwide shares. Plaintiffs have offered no case which has held that more is required. On the other hand, defendants point out numerous cases, decided subsequent to the promulgation of Rule 13e-3, where proxy statements were upheld, containing no more detailed discussions of net book value, liquidation value, and going concern values than the discussion contained in the proxy statement in question. *Radol v. Thomas*, 534 F. Supp. 1302, 1315-17 (S.D. Ohio 1982); *Berg v. First American Bankshares, Inc.*, [1984-85] Fed. Sec. L. Rep. (CCH) ¶ 92,011 (D.D.C. 1985); *Nutis v. Penn Merchandising Corp.*, 610 F. Supp. 1573 (E.D. Pa. 1985). Rule 13e-3 "merely requires that an opinion be given and the material factors on which it is based be disclosed." *Radol*, 534 F. Supp. at 1316. We conclude that defendants satisfied this requirement of Rule 13e-3 by listing the factors considered by the Evaluation Committee and by candidly stating that no specific weight was given to

any one factor, but of particular importance in the consideration was First Boston's opinion and the fact that the merger price represented a premium over the market price of the stock.

Plaintiffs strongly urge that Nationwide was required to discuss the fact that "significant balance sheet items, even though reported in accordance with GAAP, actually understate the assets, understate the liquidity of the company, and overstate liabilities by significant amounts." Plaintiffs contend that Nationwide was required to disclose that most life insurance companies are valued substantially in excess of book value or net asset value because GAAP reporting tends to understate net asset and liquidity values. Plaintiffs have not offered any authority which would require defendants to make such a disclosure. Moreover, we are persuaded by the fact that Peat, Marwick, Mitchell & Co., independent outside auditors, reviewed the financial information contained in the proxy statement and opined that "such financial statements present fairly the financial position of Nationwide Corporation and its subsidiaries, . . . in conformity with generally accepted accounting principles applied on a consistent basis." We are further persuaded by the testimony of plaintiffs' own expert who stated that he was unable to single out anything about the financial information which was inaccurate or misleading (Clark deposition, p. 153). From the foregoing, we conclude that the proxy statement adequately set forth the net book, liquidation, and going concern value of Nationwide shares.

Plaintiffs' second contention relating to the "fairness" requirement of Rule 13e-3 is that Nationwide should have disclosed that the stock was "thinly traded." We disagree. The proxy statement disclosed that Nationwide Mutual owned 85.6% of the outstanding Class A shares, the number of publicly held shares, the number of public stockholders, and that the stock was traded only in the "over-the-counter market." We are mindful of the uni-

versal rule that a proxy statement need only set forth the full and fair picture, without interpretation or characterization, so that a reasonably prudent stockholder can make an intelligent decision, whether the question arises in a suit brought under §§ 14(a) or (e) or 10(b) and Rule 10b-5. *Santa Fe Industries, Inc. v. Green*, 430 U.S. at 474-77, 97 S. Ct. at 1301-03; *TSC Industries, Inc. v. Northway, Inc.*, 426 U.S. 438, 96 S. Ct. 2126, 48 L. Ed. 2d 757; *Golub v. PPD Corp.*, 576 F.2d 759 (8th Cir. 1978). We conclude that this statement of the law is also applicable to a claim under Rule 13e-3. While recognizing that the freeze-out merger situation requires more stringent legal disclosure requirements, *Radol v. Thomas*, 772 F.2d 244, we do not believe that the more extensive disclosure requirements should cause us to lose sight of the purpose of the proxy statement, which is to provide enough information so that the shareholder can draw his own conclusions and make his own decisions. After reviewing the proxy statement, we conclude that enough information was provided therein to allow a reasonably prudent shareholder to make his own characterization of the market for Nationwide stock.

Finally, plaintiffs argue that the proxy statement contained an inadequate discussion of the First Boston opinions, that the proxy statement should have disclosed the method utilized in determining the $42.50 price, and that First Boston never determined the intrinsic value of Nationwide or its stock. More specifically, plaintiffs contend that the proxy statement fails to set forth projected growth rates and increase of earnings. We conclude that such projections were not required to be disclosed. "[T]he law mandates disclosure only of existing material facts. It does not require . . . any economic forecasts." *Arber v. Essex Wire Corporation*, 490 F.2d 414 (6th Cir. 1974).

The most recent pronouncements by the Sixth Circuit reaffirm this basic rule in the context of Rule 13e-3. In *Starkman v. Marathon*, 772 F.2d 231, the Court stated:

> With respect to asset appraisals, Rule 13e-3, 17 C.F.R. § 240.13e-3 requires disclosure of the information called for by Items 7, 8, and 9 of Schedule 13E-3, 17 C.F.R. § 240.13e-100, in the context of freezeout mergers. Item 8 of Schedule 13E-3 requires disclosure of factors important in determining the fairness of such a transaction to unaffiliated shareholders, and these factors include liquidation value; Item 9 of that same schedule says that a summary of any outside appraisal must be furnished, with the summary including a discussion of the procedures and methods of arriving at the findings and recommendations of the appraisal. However, a 1979 SEC-proposed amendment under which an issuer would have to disclose any projection given to an appraisal furnisher was never adopted, *see* 2 Fed. Sec. L. Rep. (CCH) ¶ 23,706, at 17,245-21 through 21A, and, even more importantly, in *Radol v. Thomas*, 772 F.2d 244 (6th Cir. 1985), we have rejected the position that SEC rules regarding freezeout mergers and proxies should determine the disclosure obligations of target management in the first stage of a two-tier tender offer.

Id. at 240.

The Court, in *Starkman*, further noted that the disclosure of "soft" information such as appraisals and earnings projections is required only when "the reported values are virtually as certain as hard facts," *Id.* at 241, and that earnings and cash flow projections do not rise to the level of substantial certainty triggering a duty to disclose. *Id.* at 242 (citing *Biechele v. Cedar Point*, 747 F.2d 209 (6th Cir. 1984) and *James v. Gerber Products Co.*, 587 F.2d 324, 327 (6th Cir. 1978)). In the companion case of *Radol v. Thomas*, 772 F.2d 244, the Court specifically approved the instruction that a "failure to make known a projection of future earnings is not a violation of the Federal Securities Law." *Id.* at 252. There-

fore, we conclude that defendants were not required to disclose projected growth rates and future increase of earnings.

Additionally, plaintiffs argue that the discussion of the First Boston Opinion should have disclosed information regarding comparable life insurance companies as such information would reveal the unfairness of the cash out price. Specifically, plaintiffs contend that the shareholders should have been told that First Boston stated that acquisition of life insurance companies generally range from one to four times book value. On this point, we find the reasoning of the Court in *Gans v. Filmways, Inc.*, 453 F. Supp. 1116 (E.D. Pa. 1978) to be persuasive:

> [I]nsurance companies are not fungible entities and the value of one company is not a reliable indication of the value of another. Secondly, and perhaps more importantly, the notion of book value is of little if any help in determining the actual value of a share of stock. As Chief Judge Lord of this district has noted, the 'suggestion that book value is any indication of the real value of shares of stock has long been discredited, and should not have been resurrected for the purposes of this proxy solicitation.' Because book value has no relation to real value, it is indisputable that a reasonable investor would not consider the ratio of book value to exchange rate in other sales of insurance companies of any importance in deciding how to vote on this particular merger.

Id. at 1120 (citations and footnotes omitted).

There is no indication that there was anyone or any other entity, besides Mutual, interested in purchasing Nationwide. Therefore, the alleged omission of "comparable values" was immaterial and indeed such information may have been misleading if discussed.

CONCLUSION

From the foregoing, we conclude that defendants' proxy statement satisfied the requirements of Rule 13e-3 and explanatory schedules relating thereto. Most important, there was sufficient information disclosed in the proxy statement to enable the stockholders to make an informed decision on what to do. It is the conclusion of the Court, therefore, that there is no genuine issue of material fact concerning the adequacy of the proxy statement when measured against the standard set forth in Rule 13e-3, and that any omissions pointed out by plaintiffs were not material as defined by the Court in *TSC Industries, Inc.*, 426 U.S. at 449, 96 S. Ct. at 2132.

Having concluded that the disclosure requirements of Rule 13e-3 were satisfied, all that remains of plaintiffs' claim is actually a controversy over the adequacy of the price paid per share, which is not a cognizable claim under the Federal Securities Law. *Marsh v. Armada Corp.*, 533 F.2d 978, 979 (6th Cir. 1976), *cert. denied*, 430 U.S. 954, 97 S. Ct. 1598, 51 L. Ed. 2d 803 (1977). Moreover, since there is no evidence of any breach of fiduciary duty owed plaintiffs by defendants, and the merger was neither unauthorized by statute, illegal nor ultra vires under Ohio corporation law, the Ohio statutory appraisal right constituted plaintiffs' exclusive state law remedy. Plaintiffs have failed to avail themselves of that remedy. We note that the merger was approved by an overwhelming 94.7% of the voted public shares and no shareholder elected to proceed in the Ohio courts to determine the fair cash value of the stock pursuant to § 1701.85 of the Ohio Revised Code. We will not permit them now to pursue their state claim, disguised as a violation of federal securities law in Federal Court. Consequently, judgment shall be entered for defendants dismissing the amended complaint.

SO ORDERED.

STATUTORY AND REGULATORY PROVISIONS

Section 13(e)(1) of the Securities Exchange Act of 1934, 15 U.S.C. § 78m(e)(1) (1988) provides:

> It shall be unlawful for an issuer which has a class of equity securities registered pursuant to section 12 of this Act, or which is a closed-end investment company registered under the Investment Company Act of 1940, to purchase any equity security issued by it if such purchase is in contravention of such rules and regulations as the Commission, in the public interest or for the protection of investors, may adopt
>
> > (A) to define acts and practices which are fraudulent, deceptive, or manipulative, and
> >
> > (B) to prescribe means reasonably designed to prevent such acts and practices.
>
> Such rules and regulations may require such issuer to provide holders of equity securities of such class with such information relating to the reasons for such purchase, the source of funds, the number of shares to be purchased, the price to be paid for such securities, the method of purchase, and such additional information, as the Commission deems necessary or appropriate in the public interest or for the protection of investors, or which the Commission deems to be material to a determination whether such security should be sold.

Section 18(a) of the Securities Exchange Act of 1934, 15 U.S.C. § 78r(a) (1988) provides:

> Any person who shall make or cause to be made any statement in any application, report, or document filed pursuant to this title or any rule or regulation thereunder or any undertaking contained in a registration statement as provided in subsection (d) of

section 15 of this Act, which statement was at the time and in the light of the circumstances under which it was made false or misleading with respect to any material fact, shall be liable to any person (not knowing that such statement was false or misleading) who, in reliance upon such statement, shall have purchased or sold a security at a price which was affected by such statement, for damages caused by such reliance, unless the person sued shall prove that he acted in good faith and had no knowledge that such statement was false or misleading. A person seeking to enforce such liability may sue at law or in equity in any court of competent jurisdiction. In any such suit the court may, in its discretion, require an undertaking for the payment of the costs of such suit, and assess reasonable costs, including reasonable attorneys' fees, against either party litigent.

Rule 13e-3(b) under the Securities Exchange Act of 1934, 17 C.F.R. § 240.13e-3 (1990) provides:

(1) It shall be a fraudulent, deceptive or manipulative act or practice, in connection with a Rule 13e-3 transaction, for an issuer which has a class of equity securities registered pursuant to section 12 of the Act or which is a closed-end investment company registered under the Investment Company Act of 1940, or an affiliate of such issuer, directly or indirectly

(i) To employ any device, scheme or artifice to defraud any person;

(ii) To make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in light of the circumstances under which they were made, not misleading; or

(iii) To engage in any act, practice or course of business which operates or would operate as a fraud or deceit upon any person.

(2) As a means reasonably designed to prevent fraudulent, deceptive or manipulative acts or practices in connection with any Rule 13e-3 transaction, it shall be unlawful for an issuer which has a class of equity securities registered pursuant to section 12 of the Act, or an affiliate of such issuer, to engage, directly or indirectly, in a Rule 13e-3 transaction unless:

(i) Such issuer or affiliate complies with the requirements of paragraphs (d), (e) and (f) of this section; and

(ii) The Rule 13e-3 transaction is not in violation of paragraph (b) (1) of this section.